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Print Edition January 7th 2006

On the cover
To some an unreconstructed hawk, to some an unlikely peacemaker, Ariel Sharon has caused tumult in Israeli politics. The likely end of his political career looks bad news for the Middle East: leader

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Politics this week

Jan 5th 2006
From The Economist print edition

Israeli politics were thrown into confusion as prime minister **Ariel Sharon** suffered a severe stroke. As Israelis contemplated the prospect that he may never return to frontline politics, deputy prime minister Ehud Olmert assumed Mr Sharon's powers. See article

Iraq witnessed its bloodiest week since parliamentary elections in mid-December. At least 130 people were killed and scores more injured in a spate of suicide-bombings (which included attacks on a funeral and religious shrines) targeting the country's Shia population. See article

The ruler of **Dubai**, Sheikh Maktoum bin Rashid al-Maktoum, died while on a visit to Australia. He had presided over the rapid development of the emirate in recent years, mainly planned and inspired by his brother, Sheikh Mohammed bin Rashid al-Maktoum, who now succeeds him.

A spat between **Russia and Ukraine** over gas prices became serious when Russia turned off the taps. The rest of Europe was swiftly hit, protests erupted all round the world—and the Russians turned the gas back on. See article

Two Turkish children died of **bird flu**, the first human deaths from the new disease outside South-East Asia.

Jack Abramoff, the Washington lobbyist at the centre of a corruption investigation, pleaded guilty to conspiracy, fraud and tax-evasion charges. As part of his plea, Mr Abramoff agreed to testify in any potential indictments (which are expected soon) brought against members of Congress. See article

George Bush stepped up pressure on congressmen to extend provisions of the **Patriot Act**. Late last month, Congress agreed to a short-term extension of the legislation, which was due to expire on December 31st, until February 3rd.

Evo Morales, a leftist who won **Bolivia's** recent presidential election, visited Venezuela, where he pledged to join President Hugo Chávez in fighting “neoliberalism and imperialism”. Mr Chávez offered to give Bolivia diesel in return for farm products.

Colombia's FARC guerrillas rejected a plan for talks with the government over an exchange of its hostages, who include Ingrid Betancourt, a politician, for jailed guerrillas. Earlier, the FARC killed 29 soldiers protecting workmen eradicating coca, in the most serious attack since Álvaro Uribe became Colombia's president in 2002. See article

Jiang Weiping, a **Chinese** journalist imprisoned after writing articles about corruption, was freed, a year ahead of time, according to a human-rights group. There was speculation that the move was tied to a possible visit by China's president to America.

A suicide car bomb in Tirin Kot, the capital of **Afghanistan's** Uruzghan province, killed ten people. It was rumoured that the attack was timed to coincide with a visit by the American ambassador to the city. See article

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Business this week

Jan 5th 2006

BASF, a German chemicals manufacturer, launched a $4.9 billion hostile bid to buy **Engelhard** (the firm's management rejected BASF's initial offer). Engelhard, which is based in New Jersey, developed catalytic converters for cars in the mid-1970s. BASF thinks the market for car-emissions products is set to boom as several countries, including China, introduce tougher pollution controls for vehicles.

The bidding war continued for **Dofasco**, a steelmaker based in Canada. Germany's **ThyssenKrupp** raised its friendly offer to C$4.9 billion ($4.2 billion), matching a hostile bid from **Arcelor** that the Luxembourg-based firm increased just before Christmas.

Dow Jones, which publishes the *Wall Street Journal*, named Richard Zannino as its new boss. Many had expected that Karen Elliott House, the wife of the retiring chief executive, Peter Kann, would assume the position (she is now leaving the group). The firm has suffered more than most other media organisations from the advertising slump following the dotcom bust.

America's **Securities and Exchange Commission** published guidelines on fining companies found guilty of fraud. The regulator is responding to critics who complain of discrepancies between the amount that some firms were charged for apparently similar offences.

Eurex, the world's biggest derivatives exchange, confirmed it was in talks with exchanges in the United States about plans that would “further develop” its American operations. Rudi Ferscha resigned as the German-Swiss firm's chief executive last month following criticism of a strategy (seen to have failed) to try to compete directly with Chicago's established exchanges.

Economists pored over the minutes of December's Federal Open Market Committee meeting of America's Federal Reserve. Much was made of the fact that “views differed” among members over how much further to tighten monetary policy. The runes pointed to another **interest-rate** rise of one-quarter of a percentage point at the next FOMC meeting on January 31st.

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CLASSIC
PERTH 2006

Israel without Sharon

After Sharon

Jan 5th 2006
From The Economist print edition

The death or departure of Israel's superhawk will darken hopes for peace

AP

SO HISTORY repeats itself after all. For the second time in the modern history of Israel, a tough and popular leader who had come to see the need for compromise with the Palestinians appears to have been cut down in mid-stride. Ariel Sharon may yet survive the massive stroke that felled him on January 4th. But even if he does, his chances of remaining prime minister and delivering the massive victory his new Kadima party was expecting in Israel's general election in March look remote. Like the assassination of Yitzhak Rabin in 1995, this could revive the prospects of Israel's bedraggled hawks and make the path to peace still harder.

Many non-Israelis, and especially the Palestinians, will find it hard to accept the notion that Mr Sharon's departure could be bad for peace. Even before earning notoriety as the architect of Israel's invasion of Lebanon in 1982, Mr Sharon had established himself as a superhawk. As a young officer in the 1950s he gained a reputation for trigger-happiness as commander of Israel's cross-border "retaliation" raids. After the Lebanon war, he was forced out of his job as Menachem Begin's defence minister after a commission of inquiry found him indirectly responsible for allowing a Christian militia to massacre hundreds of Palestinians in Beirut's Sabra and Chatila refugee camps. As housing minister in the 1990s, he was responsible for building many of the Jewish settlements in the occupied West Bank and Gaza strip. And in 2000, his provocative walk on Jerusalem's Temple Mount is said to have sparked the second Palestinian *intifada* and so delivered a fatal blow to Bill Clinton's attempts to broker a peace settlement between Ehud Barak and Yasser Arafat. Most Arabs reacted with scorn in 2002 when George Bush called him "a man of peace". The Arab media more often calls him a war criminal.

Only hawks can make peace

For all that—and like Rabin before him—Mr Sharon seemed this past year to offer Israelis a unique mixture of qualities. On the one hand, and specially after leading a ruthless counter-insurgency fight against the *intifada*, his credentials as a security hawk could not be challenged. On the other, he claimed to accept the need for Israel to make painful territorial concessions and permit the emergence of an independent Palestine. Last August came proof that this was not just talk. Unfazed by the resistance of his own ruling Likud party, Mr Sharon evacuated all of Israel's settlements from the Gaza strip. No one knows whether following up on the West Bank formed part of his thinking. But the fence he started to build around the West Bank has always looked like an attempt to mark out a political border as well as a security barrier. Such a border would give Israel 15% or so of the West Bank. That is still unacceptable to the Palestinians, but to Israelis on the national-religious right, offering up 85% of divinely promised "Judea and Samaria" is a betrayal verging on apostasy. When the rightists in the cabinet mutinied, Mr Sharon simply broke with them, quit the Likud, and formed his brand-new Kadima party.

Even by the standards of Israel's volatile and fractious democracy, this was a colossal gamble. But until this week's stroke it seemed to be working. A party of the centre, ready for a two-state solution but tough on security, is just what the secular Israeli mainstream seems to want. Opinion polls suggest that with Mr Sharon at its helm, Kadima would have trounced Likud at the election in March. The question now is whether it could do so without its paramount leader. So new is the party that Mr Sharon had not nominated his ministers and lieutenants before going into hospital. No natural successor stands out. Israel's acting prime minister, Ehud Olmert, is a capable politician who thinks along Mr Sharon's lines, but lacks a national following. Shimon Peres, who defected from Labour to Kadima, is a serial loser of elections and widely distrusted. As in 1996, in the first election following

Rabin's assassination, it is not impossible that the disappearance of a tough leader of the centre will make way for the return of a coalition led by the Likud. As in 1996, the Likud happens once again to be led by Binyamin Netanyahu, who after winning that election did much to delay and ultimately derail the Oslo peace process. And this time, following the creation of Kadima, the Likud is even less a party of the centre than it was a decade ago.

Meanwhile in Palestine...

The vacuum that Mr Sharon's departure would now create at the centre of Israeli politics makes it hard to imagine how there can be any swift progress in peacemaking with the Palestinians. What is worse is that politics in the Palestinian camp is, if anything, in even greater disarray. Mahmoud Abbas, the man the Palestinians elected president after the death of Mr Arafat just over a year ago, has proved incapable of administering either the West Bank or the recently evacuated Gaza strip. In parliamentary elections later this month, the violent Islamic extremists of Hamas are expected to do very well. Israel says that if they join the government of Mr Abbas's shambolic Palestinian Authority, it may cut off what little contact it still maintains with the Palestinian leadership and suspend its already largely nominal compliance with the international “road map” for peace. A final worry is that the self-imposed year-long period of calm that has lately taken the steam out of the Palestinian *intifada* has just come to an end. An abrupt escalation of violence, which would in turn strengthen the extremists on both sides, is all too possible.

It would be wrong to imply that if Mr Sharon had not suffered a stroke Israel would have marched inexorably ahead towards peace with the Palestinians. No matter who leads them, the gap between the expectations of the two peoples remains frighteningly wide. All the same, Mr Sharon's new party had seemed poised to make a breakthrough of historical significance, by mobilising the moderate majority in Israel and breaking the stranglehold of the settler movement. This remains an essential first step towards compromise. It is indeed an irony that Israel's arch superhawk looked like the man most likely to pull it off. But it is no less true for that. Without Mr Sharon, hope will darken yet again.

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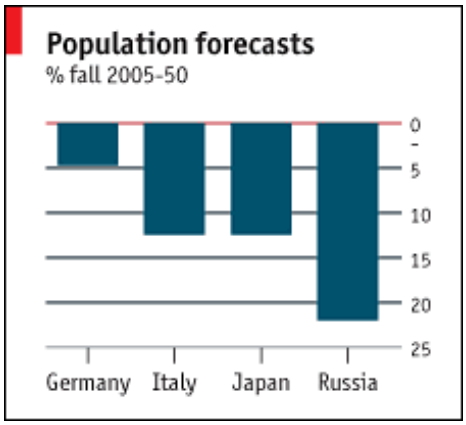
PERTH 2006

Declining populations

Incredible shrinking countries

Jan 5th 2006
From The Economist print edition

Rich countries' populations are beginning to shrink. That's not necessarily bad news



DURING the second half of the 20th century, the global population explosion was the big demographic bogey. Robert McNamara, president of the World Bank in the 1970s, compared the threat of unmanageable population pressures with the danger of nuclear war. Now that worry has evaporated, and this century is spooking itself with the opposite fear: the onset of demographic decline.

The shrinkage of Russia and eastern Europe is familiar, though not perhaps the scale of it: Russia's population is expected to fall by 22% between 2005 and 2050, Ukraine's by a staggering 43%. Now the phenomenon is creeping into the rich world: Japan (see article) has started to shrink and others, such as Italy and Germany, will soon follow. Even China's population will be declining by the early 2030s, according to the UN, which projects that by 2050 populations will be lower than they are today in 50 countries.

Demographic decline worries people because it is believed to go hand in hand with economic decline. At the extremes it may well be the result of economic factors: pessimism may depress the birth rate and push up rates of suicide and alcoholism. But, in the main, demographic decline is the consequence of the low fertility that generally goes with growing prosperity. In Japan, for instance, birth rates fell below the replacement rate of 2.1 children per woman in the mid-1970s and have been particularly low in the past 15 years.

But if demographic decline is not generally a consequence of economic decline, surely it must be a cause? In a crude sense, yes. As populations shrink, GDP growth will slow. Some economies may even start to shrink, too. The result will be a loss of economic influence.

Governments hate the idea of a shrinking population because the absolute size of GDP matters for great-power status. The bigger the economy, the bigger the military, the greater the geopolitical clout: annual GDP estimates were first introduced in America in the 1940s as part of its war effort. Companies worry, too: they do not like the idea of their domestic markets shrinking. People should not mind, though. What matters for economic welfare is GDP per person.

The crucial question is therefore what the effect of demographic decline is on the growth of GDP per person. The bad news is that this looks likely to slow because working-age populations will decline more rapidly than overall populations. Yet this need not happen. Productivity growth may keep up growth in GDP per person: as labour becomes scarcer, and pressure to introduce new technologies to boost workers' efficiency increases, so the productivity of labour may rise faster. Anyway, retirement ages can be lifted to increase the supply of labour even when the population is declining.

People love to worry—maybe it's a symptom of ageing populations—but the gloom surrounding population declines misses the main point. The new demographics that are causing populations to age and to shrink are something to celebrate. Humanity was once caught in the trap of high fertility and high mortality. Now it has escaped into the freedom of low fertility and low mortality. Women's control over the number of children they have is an unqualified good—as is the average person's enjoyment, in rich countries, of ten more years of life than they had in 1960. Politicians may fear the decline of their nations' economic prowess, but people should celebrate the new demographics as heralding a golden age.

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Energy security

Power games

Jan 5th 2006
From The Economist print edition

Some countries want to use energy as a political weapon. That is harder than it looks

Getty Images

FOR a man such as Vladimir Putin, who calls the collapse of the loathsome Soviet Union the greatest geopolitical catastrophe of the 20th century, using Russia's energy riches to pamper or punish its former vassals according to whim must seem like a natural thing to do. But the decision of Russia's president this week to cut off gas supplies to Ukraine over a price dispute, on the very day he became president of the G8 rich-nations group, was a shock nonetheless. And although Russia resumed supplies after only two days, following an outcry from the wider world, it sent shivers far beyond eastern Europe. Is the "oil weapon" of the 1970s—the withholding of energy for political ends—coming back in a new guise?

Russia says it is simply asking Ukraine to pay the market price for its gas, not the subsidised rate it paid as a former Soviet satellite. But by seeking to quadruple the price for democratic Ukraine (and not, for example, for the pro-Russian dictatorship in Belarus), Mr Putin looks to be punishing the Ukrainians for having taken a pro-western direction. And it is not just Ukrainians who were put at risk. By pumping less into Ukraine, Russia also hurt customers in central and western Europe, at the pipeline's other end. It was their anger—and immediate complaints from America and the European Union—that caused the Russian climbdown.

The affair has given a new spin to what were already intense global anxieties over energy security (see article). One reason for the present twitchiness is a tight market for all forms of energy. High prices, and the absence of the usual cushion, have made the global economy vulnerable to disruptions, be they natural disasters such as Hurricane Katrina or political fumbles such as Russia's in Ukraine. Adding to the nervousness is the conviction of some producers that controlling supply offers a path to national greatness. Mr Putin plainly believes this. So does Hugo Chávez, Venezuela's president, who proposes to use oil as a weapon against the United States and to spread his "Bolivarian" revolution. And there is also a longer-term worry about the depletion of energy resources when two new industrial powers, China and India, are rising.

On the face of it, dangers galore. But look closer. The oil market is tight, but price is a wondrous mechanism, and rising prices have spurred investment. Oil production may increase in 2006, and start to reflate that missing cushion. Though high prices may persist for several more years, the danger of disruption will recede. As for using energy as a weapon, this week's Ukrainian affair is a reminder of an old lesson: that sellers depend on buyers just as much as buyers on sellers. With oil, as Mr Chávez well knows for all his huffing and puffing, aiming this "weapon" is especially difficult, since oil, unlike gas, can be loaded on tankers and sold into a single world market. As ever, the Middle East is volatile. But as we report in a survey, Saudi Arabia, the biggest producer, has for now seen off an al-Qaeda insurgency and looks poised for a period of prosperity and reform under a new king.

China's growth is sucking in energy. In 2003 it overtook Japan to become the world's second-biggest consumer of oil after America. Energy security therefore plays a growing part in China's foreign policy. China is making alliances with oil producers regardless of the democratic or human-rights credentials of these regimes. That has already brought conflict with America. The Chinese are helping to prevent Sudan and Iran from being held to account by the UN Security Council for suspected genocide in the one case and nuclear cheating in the other. With two-thirds of the Gulf's oil exports already flowing to Asia, America will face more such challenges. But though this will be a source of friction, it need not be the catastrophe some think inevitable as the established superpower and the rising one fight it out for a dwindling resource.

In fact, oil independence is a chimera for America and China alike. Both have an interest in the security of the Gulf—but also in depending less on its oil. If the Ukraine story has a moral, it is that energy security depends on the existence of a global market free from political interference, plus maximum diversity of supply. But where energy is concerned, China distrusts the market, putting greater store on state-to-state deals and the direct control of foreign supplies. By scaring off CNOOC, a state-owned Chinese oil firm that wanted to buy America's Unocal last year, America foolishly strengthened this mercantilist instinct. Meanwhile, by failing to impose the carbon tax that

would present consumers with the real cost of energy, America rejects the best way to kick its own addiction to oil and make greater use of alternatives. What a pity.

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After Jack Abramoff

It's corruption, stupid

Jan 5th 2006
From The Economist print edition

A last chance for the Republican leadership to clean house

AP

THE Republicans may dominate most of America's government, but their prospects in this year's mid-term elections look increasingly dicey. George Bush has no shortage of familiar problems—from a botched war in Iraq to the fuss over wiretapping (see article). But none has more potential to topple the conservative movement he leads than corruption.

The case of Jack Abramoff—the super-lobbyist who pleaded guilty to sundry crimes this week—is a nightmare for the Republican establishment. To begin with, it is much easier to follow than most such scams. Here is a Beltway Bandit whose banditry was so obscene that it shocked even other Beltway Bandits. Mr Abramoff charged various Indian tribes—innocent in the ways of Washington but newly enriched by casinos—around $80m in lobbying expenses and used his ill-gotten gains to build an empire of influence. Millions flowed to favoured lawmakers in the form of Scottish golfing holidays, food and booze in swanky Washington restaurants (one of which Mr Abramoff owned), tickets for sports events and sundry other perks. All the while, Mr Abramoff celebrated his own amorality, referring to his clients as “morons”.

The Abramoff affair, the biggest corruption scandal for a generation, will surely entangle some Democrats. But most of those caught up in his affairs, however innocently, are Republicans. Tom DeLay, the former majority leader already under indictment in Texas for campaign-finance irregularities, was one of Mr Abramoff's golfing buddies. Michael Scanlon, Mr Abramoff's partner in crime, who has already pleaded guilty, used to work for Mr DeLay. There are also plenty of congressmen and senators scuttling to explain and return donations.

The danger is that, as with the cronyism exposed by Hurricane Katrina, Mr Bush and his lieutenants will claim this as a case of a few bad apples. In fact, the Abramoff affair is a case study of how the conservative movement has gone wrong.

Mr Abramoff originally arrived in Washington as one of the young conservative idealists who wanted to shrink government and drain the Washington swamp. He supported Newt Gingrich's crusade to get rid of the ruling Democrats' “culture of corruption”. Nowadays, Mr Abramoff, like so many other Gingrich revolutionaries, has been engaged in influence-peddling on an epic scale. Rather than trying to cleanse K Street, the capital's lobbying centre, the Republicans had a “K Street project” to conservatise the industry.

This has produced millions for the Republican Party. But much has been lost in the process. Gone is the enthusiasm on the American right for slimming government. Under the free-spending Mr Bush, everybody has become a “big-government conservative”. Gone, too, is any enthusiasm for term limits; indeed, most Republicans spend their time trying to gerrymander districts to keep them there for life. And there is little willingness to change. You might have imagined, for instance, that the fury about money going to build two “bridges to nowhere” in Alaska in the wake of Katrina would have scuttled the projects. But the bridges are going ahead.

For the Republican establishment, Mr Abramoff's plea is a final warning to clean house. In Mr Bush's case this means not just purging the White House of cronies (he has less sway in Congress), but also vetoing spending bills. The number of “pork-barrel projects”—ones that get round normal budget rules—increased from 2,000 in 1998 to 14,000 last year. The political cost of inaction could be high. Most Americans long ago made up their mind on the Iraq war and they actually agree with Mr Bush on the wiretapping fuss. But there is no surer way of losing elections than sleaze.

This creates an opportunity for the Democrats, though it is hard to see them taking it. Their party notably lacks a Savonarola, even a flawed one like Mr Gingrich. Their main objection to pork is that it has been diverted to Republican causes, not their own. The man who has shown most enthusiasm for tackling corruption is John McCain, a Republican senator who has railed against Mr Abramoff's ilk for years and tried (not always successfully) to change the rules to make the exchange of favours for votes more difficult. Mr McCain, who still harbours presidential ambitions for 2008, may yet prove to be the big winner from the current mess. Good luck to him.

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Germany's Mannesmann affair

The trials of Josef A

Jan 5th 2006
From The Economist print edition

A new trial for the head of Germany's biggest bank should unsettle investors as well as bosses

Reuters

EVERY now and again, a rumour does the rounds in Frankfurt that Deutsche Bank is planning to move its headquarters from Germany's financial capital to London or New York. Germany's biggest bank ritually restates its loyalty and the story dies down. However, such are the occasional frictions between Deutsche Bank's ways and the corporate traditions of its homeland that its bosses must sometimes be tempted to unscrew their nameplate and go. They could be forgiven for feeling that way now, following the ruling just before Christmas by Germany's federal appeal court that the bank's chief executive, Josef Ackermann, and five other men must stand trial for a second time.

Mr Ackermann's troubles have nothing to do with his tenure at Deutsche Bank, where he has been a successful though far from flawless leader (see article). They stem instead from the hostile takeover in early 2000 by Britain's Vodafone of Mannesmann, a German telecommunications company on whose supervisory board Mr Ackermann sat. Mannesmann's management resisted Vodafone's bid stoutly, extracting much more generous terms from the British that were worth many billions to their shareholders. The result looked to many like a German embrace, for better or worse, of Anglo-Saxon capitalism: a successful, but fiercely fought, hostile bid, in which the views of institutional shareholders were in the end decisive. The rewards paid to Mannesmann's bosses after the dust settled (approved by Mr Ackermann and the supervisory board), had an Anglo-Saxon ring to them too: €57m ($55m) in all—a lot of money to be sure, but a small fraction of the extra shareholders gained from Vodafone's successful higher offer.

In America or Britain, these bonuses might have raised a few eyebrows and caused a whistle or two. In Germany, said prosecutors, they were illegal: Mr Ackermann and his colleagues had no business to approve them. The company was not contractually obliged to pay its executives so handsomely and, since they were leaving, the payments could not be construed as incentives. A trial ensued. In July 2004, a court found that securities law had been breached, but not seriously enough to warrant conviction, and the men were acquitted. The prosecutors, though, appealed and have now won a fresh trial. Although the prosecutors still have to prove their guilt, the appeal court's presiding judge hardly sounded sympathetic to Mr Ackermann and the rest, calling the payments “an irresponsible waste of company money”.

Sorry, I'm out of the office

All this, of course, is unsettling for Mr Ackermann and his bank. Although he is determined to keep his job, the prospect of a time-consuming second trial is an unwelcome distraction at best. And a guilty verdict, even if it did not mean a prison sentence, would surely make his position untenable.

However, the legal to and fro ought to be as disturbing for investors in German companies as it is for their bosses. After Vodafone bought Mannesmann, they might have assumed that the market for corporate control in Germany was starting to work much as it does in America or Britain. Now they cannot be so certain. At the very least, members of German boards would do well to be much better briefed and prepared when dealing with takeovers than Mr Ackermann and his colleagues appear to have been.

But there is a lesson for German policymakers too. At the end of this case, they should make sure that investors

and managers know where they stand. If after-the-fact rewards for extracting high prices from bidders are illegal, or if clear limits on them are to be set, so be it. But this could hurt the very interests that prosecutors are supposed to be protecting. If managers of listed companies see little gain in fighting a hostile bid, no one should be surprised if they choose a quiet life. Friendly mergers and alliances are much less bother, especially if less heed can be paid to shareholders (including small ones).

Some German politicians may take comfort from the potential buttressing of a traditional German form of capitalism. Maybe they shouldn't. Corporate control, like anything that can be bought and sold, has a habit of ending up with those who value it most. If shareholders in listed companies decide that juicy takeover battles are less likely than they were, they may be more willing to sell. That could be good news for the foreign private-equity firms now running the rule over much of German business—ironically the very groups that ignited a row last year when they were accused of being predatory “locusts”. Much more than Mr Ackermann's job is at stake.

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On farming in France, Cuba, abortion, Canada, Santa Claus

Jan 5th 2006
From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG
FAX: 020 7839 2968 E-MAIL: letters@economist.com

Foodies for France

SIR – It was good to read a balanced assessment and critique of Europe's common agricultural policy instead of the usual visceral, blanket rejection of the very principle of support for agriculture in general and for French farmers in particular ("Europe's farm follies", December 10th). If one remembers the rumpus surrounding the mere suggestion that the British beer-drinkers' pint should be replaced by half a litre—a step that would affect neither the quality nor the availability of the product—France's support for farming seems more than justifiable on the "way of life" grounds you pinpointed. This aspect of France's identity is appreciated as much by the country's numerous foreign residents and visitors, not least the British, as it is by the French themselves.

Martin Weston
Strasbourg

SIR – There is no reason why France shouldn't indulge its romance with farming if it believes this to be the foundation of its splendid regional gastronomy. But France should not require other EU member states to pay for their traditions. Instead, members should have more discretion about how much they spend on farming. This approach, known as voluntary co-financing, would allow Britain and many new members to invest funds in their knowledge-based economies that would otherwise be wasted on agriculture.

Michael Davies
London

Cuba libre

SIR – It is ridiculous for Spain to be "complaisant" with Cuba's lack of political freedom ("An unsilenced voice for change", December 17th). The first scientific survey on public opinion in Cuba since the revolution, conducted by Solidaridad Española con Cuba, a Spanish NGO, shows that around 50% of Cubans have a favourable position towards Oswaldo Payá, a prominent dissident. Moreover, a majority believe that Cuba's most fundamental problems are still domestic, such as low wages and lack of employment. Only 26% think the American embargo is the most important problem facing the country. Spain's government is putting its views on American foreign policy above the will of Cubans themselves.

Luis Zemborain
Freedom House
Washington, DC

Abortion's legal status

SIR – Lexington states that "the constitution is as clear about the right to vote— thanks to the equal protection clause—as it is murky on the right to abortion" (December 10th). This is untrue. The equal protection clause says not one word about voting. And while voting is protected against discrimination elsewhere in the constitution, the actual right to vote is explicitly protected nowhere. Moreover, to attack *Roe v Wade* because the right is unremunerated is to attack the entire edifice of modern, American constitutional rights—a result with which some conservatives might be comfortable, but with which I imagine most of your readers would not.

Ashutosh Bhagwat

Professor of law
Hastings College of the Law
San Francisco

Degrees of separation

SIR – Your survey of Canada ponders Quebec's desire for sovereignty and asks “So why does the cause endure?” (December 3rd). As someone born and raised in British Columbia, and with an according political perspective, I think you have overlooked a likely answer. Similar to a child who threatens to hold its breath until it gets what it wants, Quebec has found the threat of separation to be a wonderful tool to extract what it wants from the federal government. You seem puzzled over why Quebec would want to separate when it gets more than its fair share of federal largesse. This only confirms that the separatist threat has been an effective strategy for Quebec and inadvertently answers your own question.

Bob Carmichael
Lagoa, Portugal

SIR – I was delighted to read your well-balanced report on Quebec's sovereignty. It is a rarity in the Anglophone media. Your conclusion that “Quebec wants to be treated as an independent nation because it feels like one” is spot on. Also, your acknowledgment of the self-evident fact that, in the event of Quebec's sovereignty, “neither the United States nor the rest of Canada would have an interest in pushing [Quebec] out of NAFTA” is unheard of in the English-Canadian press.

Daniel Audet
Former agent general of Quebec in London
Montreal

SIR – You used a photo of Charles de Gaulle waving to a crowd and placed the event in Montreal. Actually, the photo was taken in Quebec City. As I remember it, de Gaulle visited Montreal after Quebec City in 1967, and it was in Montreal that he gave his famous “*Vive le Québec libre*” speech.

Pierre Bouillon
Quebec City, Canada

SIR – The perception in your leader on Canada of the New Democratic Party (NDP) is both presumptuous and misguided (“Canada's wintry election”, December 3rd). Contrary to popular belief, the NDP has stated outright that it is pro-growth. Far from courting “old socialist” candidates, it has attracted the likes of Paul Summerville, former chief economist for RBC Dominion Securities. Unlike the Liberals and Conservatives, the NDP believes that innovation strengthens our public institutions and can make Canada become more competitive. One example is a plan to retrofit every building in Canada and so reduce our greenhouse-gas emissions, thus drastically cutting Canada's energy bill. And that, to paraphrase your newspaper, is just one of the reasons why more than 2m Canadians consider the NDP to be “cool”.

Michael Hurley
London, Canada

SIR – By describing Canada as a “frozen waste”, “provincial” and “grumpily anti-American” your patronising leader could have been written by Condoleezza Rice. Your implication is that Canada should have a more worldly and sophisticated view of its neighbour, which we formerly trusted. We are grumpy because we have learned, to our surprise and chagrin, that our trust has been misplaced and that our concept of the rule of law, from torture to trade agreements, differs radically from that of the United States.

Richard Potter
Milford, Canada

Humbug

SIR – The abuse of Santa Claus's image around the planet tells a very different tale to the one you spread in your Christmas issue—and it is a dismal one (Face value, December 24th). As with clean air or fish stocks, the lack of clearly assigned and enforceable property rights has led to a massive overuse of that most valuable commodity, the Spirit of Christmas. If Santa were truly in command of his resource, as a rational monopolist he would drastically restrict its supply.

Marco Salvi

Zurich

SIR – Thanks for the insight into the workings of Santa. Is it envisaged he will raise capital through an IP-ho-ho-ho?

Lewis Graham
Hitchin, Hertfordshire

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Criminal gangs in the Americas

Out of the underworld

Jan 5th 2006 | GUATEMALA CITY, LOS ANGELES AND SAN SALVADOR
From The Economist print edition

Corbis

Numerous, mysterious, and now spreading fast in the United States

IN THE back courtyard of a deserted wreck of a house on the outskirts of San Salvador, El Salvador's capital, a group of young men is gathered. One sleeps on a couch without cushions, under a bare light bulb, as his friends talk. Many are covered with tattoos from their forearms to their faces, marking them to all eyes as gang members. Each tattoo contains a code and tells a story. A trinity of three dots, for example, means hospital, prison and the graveyard, the three possible ends for a gangster.

These young men belong to the largest criminal network in the Americas, and one of the largest in the world. Besides an estimated 25,000 members in El Salvador, there are comparable numbers in Guatemala, Honduras and the United States. The distinctive graffiti found scrawled in Central America are indistinguishable from those in the *barrios* of Los Angeles—and as far east, these days, as the suburbs of Washington, DC.

Where traditional organised crime, such as the Colombian or Mexican drug “cartels”, tends to be organised in small, elite groups, this network, based round gangs, is larger and more diffuse. Its business is extortion and drug-trafficking. In El Salvador, Guatemala and Honduras it accounts for between 20% and 50% of all violent crime. In the United States, authorities believe members are responsible for much of the smuggling of people and goods across the border with Mexico.

Two *maras*, or gangs, are involved, Mara 18 and Mara Salvatrucha. Though they are bitter rivals, their methods and interests are the same. To some observers, their members are as much a threat to America as al-Qaeda. Indeed, links have been suspected, though there is no evidence for them. The FBI has struggled fruitlessly to convince Americans that one particular meeting between Adnan G. El Shukrijumah, an al-Qaeda lieutenant, and members of Mara Salvatrucha is pure myth. One recent Republican candidate for governor of Virginia made that “meeting” a cornerstone of his stump speech against crime.

More realistically, the *maras* are feared for their fast-growing numbers, their reputation for unusual violence (in Central America, beheadings are not unheard of as a means of execution) and their appearance in new, far-flung areas of the United States. California has been dealing with the gangs for over 20 years, but as Chris Swecker, assistant director of the FBI, told a congressional hearing on the *maras* in 2005, *mareros* have now migrated and proliferated “in many smaller, suburban and rural areas not accustomed to gang activity and related crimes.” In

2003 Brenda Paz, a pregnant 17-year-old federal witness, was found stabbed to death on the banks of the Shenandoah river in deepest Virginia.

Yet the young men in the courtyard in San Salvador, members of Mara 18, or the 18th Street Gang, do not look threatening at all. They seem abject and scared. Not only are they unemployable, but they can no longer walk openly in the street outside their neighbourhood. A series of tough laws passed over the past few years has stiffened penalties even for belonging to a gang (although some provisions were struck down in court as unconstitutional), and police have adopted a get-tough policy which, even if it has not succeeded in reducing crime, has at least frightened gang members. Their new tattoos are in not-very-noticeable places. “We have lost the right to exist,” says 19-year-old Oscar.

How dangerous is the phenomenon they are a part of? Neither Mara 18 nor Mara Salvatrucha (also known as MS-13) is well understood. The origins of both are shrouded in disagreement. Gang members themselves do not keep a history or, if they do, do not share it with outsiders. Some police say the gangs were founded in El Salvador in the 1970s or earlier. Others say they sprang out of the Salvadoran immigrant community in central Los Angeles in the early 1980s. Salvatrucha may have been founded by a group who had been kicked out of Mara 18, which was run at first by Mexican immigrants in Los Angeles. Alternatively, Mara 18 was founded by a group of renegade Salvatruchas.

Some experts claim that both have developed command and control structures. Some say that their component “cliques”, which range from ten to 100 gang members, function as franchises; others insist that they are not very organised at all. Certainly the movement of money within the gangs seems mysterious. Both gangs extort from small businesses, taxi drivers, homeowners—almost anyone passing through their neighbourhoods. Both sell drugs. These are both highly lucrative enterprises. But most members seem to be poor.

One American official in Guatemala estimates that in Villanueva, a suburb of Guatemala City, gangs pull in at least $100,000 a week. He assumes that much of this money must be sent to the United States, since gang members in Guatemala, as in El Salvador, appear to be living on the edge of subsistence. But Jody Weis, an agent with the FBI in Los Angeles, says that gang members there are poor, too, and suspects they are sending money to Central America. Anyone who tries to “follow the money” is soon lost. But it is likely that the *maras* are making much less than the authorities believe.

Unequal shares

According to Oscar, the *marero* in San Salvador, the *mara* is like a family. Members take care of each other and retaliate if attacked, but nothing more. According to Salvadoran police officials, any *marero* with tattoos must have murdered someone in an initiation rite. Oscar and his friends clearly live on the margins of society; but they do not look much like murderers.

Nonetheless, a lot of murders happen. The murder rate in 2004 was 46 per 100,000 people in Honduras; in El Salvador it was 41, in Guatemala 35. In the United States, by contrast, it was 5.7, with the Mexican rate roughly double that. El Salvador and Guatemala are both still recovering from the legacy of decades-long civil war—one possible explanation for the high rate of violence. Honduras, the country worst affected, suffered a “dirty war” in the 1980s. But Nicaragua, which also suffered a long civil war, does not have comparable gang problems. *Maras* are not widespread in Belize, in Costa Rica, or in Panama. Why El Salvador, Guatemala and Honduras have tens of thousands of *mareros*, and their neighbours almost none, is a mystery that no one can answer.

The only consensus among the authorities is that things are getting worse, and that this deterioration has been particularly pronounced over the past four to five years. José Miguel Cruz of the University of Central America, in San Salvador, ascribes this to the get-tough policies of the government. *Mareros* clapped in jail have had nothing to do but organise, and so the gangs have became stronger and more violent. The first 11 months of 2005 saw 23% more murders in El Salvador than in all of 2004. Comparable increases have been seen in Honduras and Guatemala. Mr Cruz also points out, anecdotally, that of 20 gang members he enrolled in a long-term study in 1996, only five are still alive.

This rise in violence is having a serious impact on Central American economies. According to a study by the United Nations Development Programme (UNDP), the cost of violence to El Salvador in 2003 was $1.7 billion, equivalent to 11.5% of GDP. The Inter-American Development Bank is even more pessimistic, estimating that the per capita GDP of the region would be 25% higher if the rates of violence were no worse than the world average. Furthermore, because the rich have private security—an economic cost in itself—extortion, which can be as little as a few dollars per person per week, most affects those who can least afford it, stunting economic growth and reinforcing persistent inequality. Guatemala has one of the widest gaps between rich and poor in the world.

Of the countries with large numbers of *mareros*, the best equipped to deal with the problem is the United States.

But although there is a certain amount of co-operation, particularly with El Salvador, American policy tends to make the problem worse for its neighbours.

According to Kevin Kozak of the Immigration and Customs Enforcement (ICE) agency, 30% of gang members picked up by his agency in America are arrested and criminal charges are placed against them. But the other 70% are deported. There is no alternative; they are in the United States illegally, but evidence does not exist to prosecute them for any specific crime. Each week, therefore, dozens of gangsters are flown out by the American government on private jets and released on to the streets of Central America.

To some extent, this process is now co-ordinated with Central American governments. But it is awkward. Officials in El Salvador say they cannot ask the United States to stop the deportations, but nor can they cope with them on any large scale. If even a self-admitted gang member gets off a plane in San Salvador or Tegucigalpa, but there is no evidence to try him for a crime, he has to be allowed to walk free.

The relatively new anti-gang laws in El Salvador and Honduras do not include versions of America's witness-protection programme or its anti-racketeering laws, which allow suspects to be charged with conspiracy to commit a criminal act, rather than the act itself. In most cases, therefore, the *marero* freshly deported from Los Angeles is free to organise on his home turf—with all the prestige, preparedness and sophistication he has picked up in the United States.

In the United States itself, says Mr Weis of the FBI, law-enforcement authorities are now trying to use techniques developed against the Sicilian Mafia to fight the *maras*. However, to get an indictment, evidence is needed. And even with a witness-protection programme in place, it is very difficult to find informants. Typically, the FBI manages to recruit as informants roughly one in three of the people it approaches. With the Salvatruchas, says Mr Weis, the number is closer to one in 20.

Off the street, on the web

The gangs he encounters are also organised and sophisticated. They use throwaway mobile phones, which are essentially untraceable, and keep in touch on the internet. (Mara 18 maintains a website at www.xv3gang.com; Salvatrucha's website has been offline recently.) Frank Flores, head of the Hollywood sector of the anti-gang task-force of the Los Angeles Police Department (LAPD), points out that the *maras* now rarely deal drugs on the street in Los Angeles. They give that dirty work to immigrants whom they have brought to the country illegally, men who are ignorant both of the gang's structure and of its members' identities, and use them much like indentured servants. If they are caught, the gang is not compromised; if they are not, the revenue continues to come in.

America's campaign against these gangs is less organised than one might suppose. The various agencies involved—the FBI, ICE and local police departments—co-operate to some degree. An operation called Community Shield, led by ICE and enforced by the LAPD and the New York Police Department, led to the arrest of 103 Salvatruchas in February and March 2005 and another 582 gang members last August. However, information-sharing leaves much to be desired.

Mr Flores is proud of Calgangs, a database which uses digital photographs and other information to track gang members; but national law-enforcement officers have no access to it. Calgangs stores the details of 928 Salvatruchas, a tiny fraction of the estimated size of the gang; and more information sits, unread, on file-cards in cabinets in Mr Flores's office. He lacks the staff to sort through it. Moreover, of the four detectives in the anti-gang task-force, only two speak Spanish. Of the 12 uniformed officers, only one does.

This is in Los Angeles—a city where the *maras* arguably originated, and which has a large Latino population. Local police elsewhere in the United States are even less prepared to deal with the *maras*, says Mr Flores, who has been teaching police in other jurisdictions about the gangs. The Washington, DC area, which has the second-largest concentration of *maras* in the country, is approximately where Los Angeles was ten years ago, says Mr Flores. Everywhere, the statistics on gang-related crime are not remotely reliable. The same fear that makes it difficult to recruit informants means that most gang crime goes unreported.

At least, in the United States, the arrests that are made may make some small difference. The gangs continue to organise in prison, but jailhouse murders are relatively rare, and the state retains some control over the penal system. In Central America, that is not the case. In 2005, says Douglas Omar García Funes, subdirector of investigations for the Salvadorean national police, an average of two to three *mareros* were killed in jail each day. In October 16 escaped, a typical number. The gangs, says Mr Funes, dominate the jails.

The warden of Tonacatepeque, a youth prison (with inmates aged 13 to 24), agrees with him. Although the prison is surrounded by an imposing 20-foot fence, and the warden claims his methods are more or less effective, he

admits that the gang structure exists unchanged inside the prison. When he wants to search the cells, all the inmates are led out to a field in their underwear in the early morning, as he would not risk a search with inmates present for fear of losing control. Beat Rohr of the UNDP puts it more plainly: “The jails are nothing more than schools of crime.”

Indeed, across the affected Central American countries, the prisons are often segregated between the two rival *maras*, as authorities have been unable to keep control when members of both gangs are under the same roof. In August 2005, a long-standing truce between the Salvatruchas and Mara 18 in Guatemala—holding even though the two were still at odds in El Salvador and Honduras—was broken when at least 35 Mara 18 members were killed by Salvatruchas in a co-ordinated effort across several Guatemalan jails.

“We cannot”, says Paul Vernon of the LAPD, “arrest ourselves out of the gang problem.” This is something that the Guatemalan and Salvadorean governments have yet to realise. The victory of Manuel Zelaya in November's elections in Honduras is a good sign; Mr Zelaya was less prone to get-tough rhetoric than his opponent. Honduras has had perhaps both the worst attacks by *maras* and the heaviest-handed anti-*maras* efforts. In December 2004 a bus was attacked, and all 28 people on it murdered; the assault was thought to be, at least in part, payback for a mysterious prison fire earlier in the year in which over 100 Salvatruchas burned to death.

A better life

Gang violence in Central America is unlikely to wane in the near future. Police resources are stretched or non-existent. Rehabilitation programmes are tiny and, according to one Salvadoran official involved in the small pilot programmes, have at best a 30% success rate. Jails are stuffed to almost twice their capacity in El Salvador, and will probably remain so. Despite good intentions on all sides, effective co-operation among law-enforcement agencies—the sharing of databases, for instance—is not on the horizon. No country even has a comprehensive database of who is who among the gangsters. As police dither, the gangs also grow stronger up and down the United States.

The only real hope is that economic growth will eventually lift El Salvador, Guatemala and Honduras out of their poverty and so reduce the incentives for joining gangs. Oscar, the Salvadorean *marero*, says he would prefer to get a regular job rather than be in a criminal gang any more. But with gang violence itself acting as a brake on his country's growth, the prospect seems dim.

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The political year

Will lightning strike the Republicans?

Jan 5th 2006 | WASHINGTON, DC
From The Economist print edition

Predictions of a Democratic takeover of Congress seem premature. But the Republicans could lose their majority of governorships this year

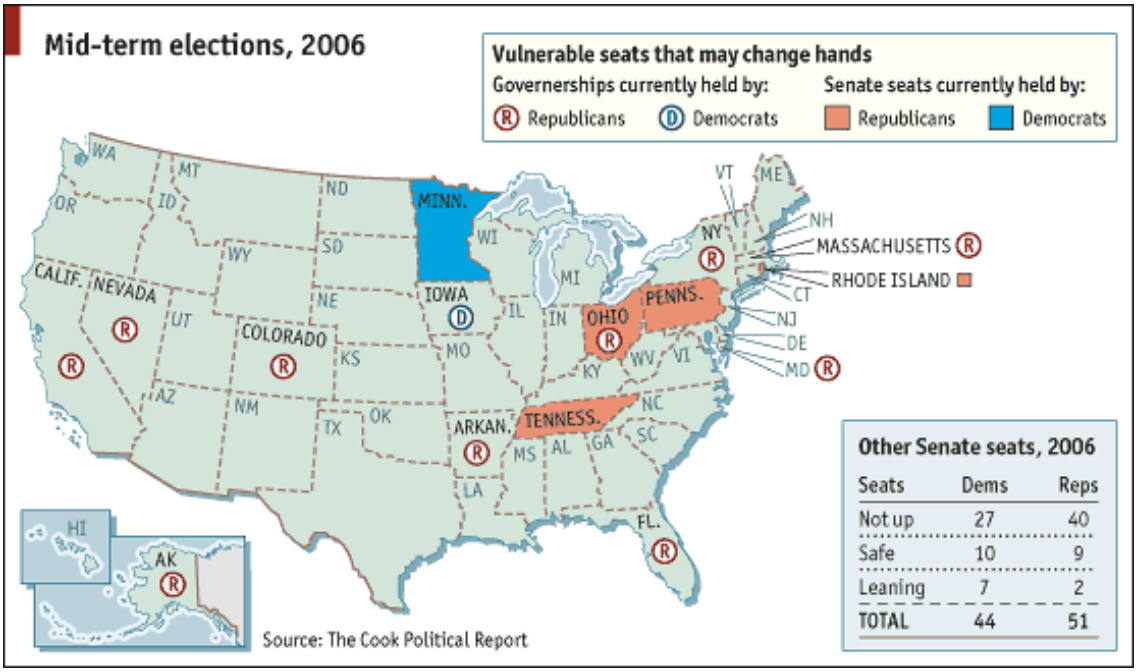
WHAT a cheery start to the new year for the Democrats. On January 3rd, Jack Abramoff, the Demon Briber of K Street, agreed to open his capacious pockets to investigators and reveal which politicians are inside (see article). Most of the red faces are expected to be Republican. The ruling party has one leg bogged down in Iraq and the other in sleaze. Democrats are now dreaming of seizing control of Congress and impeaching George Bush for his "illegal" wiretaps.

Dream on. Most analysts expect the Republicans to lose ground at the mid-term elections in November, but there are several reasons for doubting that the party's pain will translate into power for the Democrats on Capitol Hill, let alone a chance to impeach the president.

Some of the obstacles the Democrats face in November are structural. In the Senate, the current Republican majority is 55-45. Only a third of seats are to be contested this year. Of these, the Democrats currently occupy 17 and the Republicans 15 (the other is held by an independent who usually votes with the Democrats). To win an overall majority in the Senate, the Democrats would have to keep their behinds glued to all their own seats and snatch a further six from beneath the Republicans.

Charlie Cook, an expert watcher of such races, currently lists only five seats as toss-ups, with four of those defended by Republicans (see map). For the Democrats to get a majority, they would have to win all the toss-ups and both the seats Mr Cook lists as leaning Republican—Missouri and Montana. A better bet for the moment would be a net gain of just three seats.

In the House of Representatives, the Republican majority is 231-203, with one vacancy. All 435 seats are being contested. The Democrats need to gain only 15 seats to win control of the House, but that is harder than it sounds. Incumbents in the House are fiendishly hard to dislodge—in a typical election year, more than 90% of those who stand, win. This is partly because both parties have shamelessly gerrymandered districts to protect sitting congressmen, and partly because incumbents outspend their challengers by a factor of 6.6. (Why give money to someone who's going to lose, and can't return the favour?)



All in all, it will take a big shift in the public mood to hand control of Congress to the Democrats. That is not impossible. Ten months is long enough for more top Republicans to be indicted, and plenty of time for more corpses to return from Iraq. But neither issue has yet swung decisively towards the Democrats. For instance, a *Washington Post*-ABC poll in November found that 71% of respondents thought there was little ethical difference between the two parties. Some will have changed their minds since then (and probably in an anti-Republican direction) but many Democrats got money from Mr Abramoff too.

On Iraq, a slim majority of Americans think the war was a mistake, but the Democrats have failed to capitalise on this fact. The alternatives they offer range from “run away” to “carry on doing approximately what Mr Bush is already doing while reminding the public whose fault it is that we're there in the first place”. Such incoherence hardly inspires floating voters.

Even if control of Congress does not change hands, November could see the American political landscape alter in significant ways. Some powerful Republicans may well be ejected from Congress. Tom DeLay, who resigned as House majority leader in September to fight charges that he broke campaign-finance laws, looks shaky. Republicans would miss his political arm-twisting skills.

The fall of Rick Santorum, Pennsylvania's junior senator, is even more eagerly anticipated by the American left. Mr Santorum is one of America's most articulate opponents of all things permissive. His six children are home-schooled; he opposes stem-cell research; he feels that sodomy should be outlawed; he favours national service. James Dobson, the head of Focus on the Family, an evangelical group, praises his “integrity, vision and unwavering commitment to the principles and beliefs upon which the United States was founded”. Meanwhile, gay activists use his name to denote something indescribable in a family newspaper.

Unfortunately for Mr Santorum, he is more conservative than his constituents in Pennsylvania (which voted for John Kerry last year). Mr Santorum won his seat in 1994, when the Republicans hit their high-water mark. Now the tide has turned: polls show him trailing his Democratic challenger, state treasurer Bob Casey, by about ten points.

Many mansions

More attention is paid to Congress, but the Democrats' most important gains will probably come in the governors' races. The Republicans currently hold 28 governorships to the Democrats' 22, but that majority is sure to shrink and may disappear. Thirty-six of the 50 mansions are up for grabs. Mr Cook reckons ten Republican-governed states could plausibly go blue (see map). Mitt Romney, the outgoing governor of Massachusetts and head of the Republican Governors Association, warns that his party may lose as many as six, which would give the Democrats a majority of governorships for the first time since 1994.

Governors' races are more competitive partly because of term limits, which apply in several states. Rather than fighting an incumbent with 100% name recognition, challengers in such states have a chance of facing opponents as unknown (relatively speaking) as themselves. This hits Republicans harder than Democrats, because they have more mansions to defend. Of the nine governors retiring this year (voluntarily or otherwise), eight are Republican.

So the party is sure to lose some stars. Those obliged to stand down include Jeb Bush in Florida (the president's brother), Mike Huckabee in Arkansas (a presidential hopeful in 2008), and Bill Owens in Colorado (an anti-tax zealot who angered his allies by shrinking scheduled tax cuts). Those stepping aside voluntarily include George Pataki in New York (who has had enough after three terms) and Mr Romney (who is retiring to concentrate on a presidential bid). Vulnerable Republicans include Arnold Schwarzenegger in California, who has promised to run again, but whose star power has faded.

For the Democratic Party, the governors' races offer a golden chance to prove they can spread their appeal beyond the coasts. For individual Democrats, they offer a shot at national prominence. Perhaps the most interesting stage is New York, where polls suggest that Eliot Spitzer, the state attorney-general, will win.

That would be interesting, for Mr Spitzer, besides being young (he is 46), smart and boundlessly ambitious, exemplifies both his party's strengths and its weaknesses. Like so many top Democrats, he is a child of the coastal elite (his property-developer father is said to be worth $500m) and open to charges of being out of touch with the little guy. His fans, however, think him a noble crusader on the little guy's behalf. As a prosecutor, he has wrung huge settlements out of banks, power plants and other rich and powerful entities, for offences such as stiffing small investors and causing acid rain.

His critics say he deliberately targets unpopular industries to serve his political ambitions, and that he has usurped powers that properly belong to other branches of government. When pursuing Wall Street, for example, he used the threat of prosecution to force the whole industry to change the way it did business, which is surely the job of regulators. Mr Spitzer retorts that the Republican-controlled regulators weren't doing their job.

Complaints about Mr Spitzer's power-grabbing (which mirror Democratic gripes about Mr Bush's “imperial” presidency) can only grow louder if Mr Spitzer wins himself the governorship of a key state in November. But the way things are going, Republicans will have plenty of other things to fret about by then.

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A mining tragedy

Jan 5th 2006
From The Economist print edition

Getty Images

Some newspapers had already run with banner headlines, “Miracle in the Mine”. Church bells had been rung. But the news that all 13 miners trapped inside the Sago mine in Tallmansville, West Virginia, had been found alive was not true. Only one had survived. The directors of the rescue effort seem to have misinterpreted a radio message from the rescuers. Relatives were not told the truth until they had spent three hours rejoicing. This was America's worst mine accident for four years, and the worst in West Virginia since the Marion County blast of 1968, which spurred proper federal mine-safety laws. The Sago mine had been cited for safety violations more than 50 times. An investigation, announced on January 4th, will include an inquiry into how news was relayed from rescuers in the mine to the desperate families on the surface.

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Political corruption

Jack the giant-killer

Jan 5th 2006 | WASHINGTON, DC
From The Economist print edition

Who else will Jack Abramoff bring down with him?

AP

Provider of money to both Republicans and Democrats

AS A young Republican, Jack Abramoff said his plan was to remove the left from power permanently. He may end up having done more damage to the right. On January 3rd, the once-powerful lobbyist pleaded guilty in a federal courtroom in Washington, DC, to conspiracy to bribe public officials, fraud and tax evasion. A day later, in Miami, he admitted to another two counts, of fraud and conspiracy, related to a 2000 acquisition of casino boats. He is likely to serve ten years in prison and he has already agreed to pay back $26.7m.

This massive scandal began with Mr Abramoff's contemptuous treatment of the Indian tribes who were his clients. He and his business partner, Michael Scanlon, who pleaded guilty to conspiracy to commit bribery last November, persuaded tribes from Texas to Mississippi to hand over some $80m. Under the “gimme five” scheme, Mr Abramoff would refer tribes to Mr Scanlon's public-relations business, and Mr Scanlon would send half the profits back to Mr Abramoff in kickbacks that the tribes did not know about. In one case, Mr Abramoff accepted money from two different tribes to lobby for opposing sides (one wanted casinos in Texas, the other did not). He hid his gains from the Internal Revenue Service with falsified financial records.

Mr Abramoff spent a lot of the cash on currying favour with lawmakers. He took congressmen and their aides to play golf in Scotland, to watch the Super Bowl, and to eat at fancy restaurants he owned in Washington. One politician and his sidekicks got a trip to a remote Pacific island.

The gifts bought influence. By his own admission in the plea deal, Mr Abramoff “provided a stream of things of value to public officials” in exchange for official favours. Statements were inserted in the *Congressional Record* and agreements were made to support certain laws (one lawmaker, according to the plea, agreed to introduce a bill to roll back a federal ban on commercial gaming so as to help one of Mr Abramoff's tribal clients in Texas).

A contrite Mr Abramoff wants “forgiveness from the Almighty and from those I've wronged or caused to suffer”. His erstwhile friends are less concerned with his soul than with whom he will implicate. The Department of Justice has promised to prosecute aggressively.

Although roughly a third of Mr Abramoff's money went to Democrats, Republicans are especially on edge. As the

ruling party, they will be held responsible for any sleaze, and they have already had one hiccup: last November, Randy “Duke” Cunningham, a congressman from San Diego, confessed to accepting $2.4m in bribes and to evading over $1m in taxes. His inducements included a Rolls-Royce, Persian carpets and the use of a yacht.

Bob Ney, an Ohio Republican who chairs the House Administration Committee, appears to be “Representative 1” cited in the plea deal. According to the plea, Mr Abramoff channelled money to Representative 1, who put statements in the *Congressional Record* beneficial to Mr Abramoff's interests. Mr Ney stated that he “obviously did not know, and had no way of knowing, the self-serving and fraudulent nature of Abramoff's activities.”

Also in the spotlight is Tom DeLay. The former House majority leader is already in trouble in his home state of Texas where, barring high court intervention, he will face trial this year on charges related to campaign finance. He has had close political ties to Mr Abramoff, with whom he has been golfing in Scotland. Mr Scanlon, Mr Abramoff's former partner, was a former aide to Mr DeLay. So apparently was “Staffer A”, another figure cited in the plea, whose wife received $50,000 over ten months allegedly to encourage him to stop legislation involving postal-rate rises and internet gambling.

This is all unproven. But it surely dims Mr DeLay's already faint hopes of regaining his leadership post, which he lost when he was indicted in Texas. Newt Gingrich, a former House speaker, has told the *Washington Post* that his party “unequivocally” needs a new majority leader.

Some prominent figures in the conservative movement may also be regretting their friendship with Mr Abramoff. One of the people who helped him get into lobbying was Grover Norquist, a leading anti-tax conservative. Another old friend is Ralph Reed, a former leader of the Christian Coalition, whose bid to become lieutenant-governor of Georgia may suffer from Mr Abramoff's past generosity—especially since money for his anti-gambling crusades originated from Indian casinos.

Democrats are sharpening their knives. But they, too, have cause for jitters. Harry Reid, the Senate minority leader, also accepted campaign contributions via Mr Abramoff. Politicians of all parties are now returning that cash as fast as possible, but opponents will be sure to bring up the taint in this year's mid-term elections. One of the latest to take action was Dennis Hastert, the speaker of the House. This week he pledged to give to charity the $69,000 in campaign money he received from Mr Abramoff and the Indian tribes.

Will this scandal cause Washington to develop a sudden case of ethics? Cynics say that some such brouhaha comes up every decade or so; lawmakers revert to best behaviour for a bit, but are never able permanently to mend their ways. But Thomas Mann of the Brookings Institution thinks that companies may get choosier about the dollars they funnel to lawmakers. “Private companies are going to be much more reluctant to pony up funds for fear of backlash from their boards, their stockholders, and legal liability.” Politicians in both the House of Representatives and the Senate could also tighten rules about disclosure and gift-giving.

Another important question is the resolve of the Justice Department. It has been criticised for looking too political—for example, giving a green light to Texas's pro-Republican gerrymandering (over fierce objections from mid-level staff) and approving Mr Bush's secret wiretaps. But the Abramoff mess looks too delicate and well-publicised a matter for political interferers even to contemplate string-pulling. Or that, at least, is the hope.

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The mid-west

The oracle has spoken

Jan 5th 2006 | CHICAGO AND DETROIT
From The Economist print edition

Trouble in the car industry is making rustbelt politicians jittery

LIKE the eponymous site of Apollo's temple, Delphi has become a focal point for politicians hoping to divine the future—and many leaders in the upper mid-west are troubled. The Delphi in question is America's biggest car-parts maker, employing 50,000 people in the United States—more than half of them in Michigan and Ohio.

Delphi entered bankruptcy in October, and its managers are pressing the United Auto Workers union (UAW) to let the firm cut wages and benefits drastically; if they do not do so by January 20th, Delphi will ask a judge to cancel its union contracts. Its primary customer, General Motors, from which it was spun off in 1999, is desperate to avoid such a showdown. GM plans to scrap 30,000 jobs and close nine assembly plants and three processing facilities in North America over the next three years. Its rival, Ford, will announce its own slate of job cuts and plant closings this month.

This pain will be felt most intensely in the upper mid-west—especially Michigan, but also in surrounding states such as Ohio and Indiana. This region is the ancestral home of the Big Three domestic car makers—GM, Ford and the American chunk of DaimlerChrysler—whose share of American car sales has fallen by 15 percentage points over the past decade, to 58%. Although America's car industry as a whole is doing well, most of the new jobs have been created in southern states by foreign-owned firms and the smaller car-parts makers that supply them. That is small comfort in the mid-west where, according to local industry chatter, some 20 suppliers are close to bankruptcy.

Politicians in the northern rustbelt are scrambling to limit the damage. Nobody in either party really knows who will bear the brunt of the blame. The bargaining about job cuts and plant-closings pits employers against the UAW, local politicians against Congress and states against each other. By the mid-term elections in November these skirmishes will coalesce into a more clear-cut battle between Democrats and Republicans, but it is not clear which issues will be to the fore: health-care reform or state taxes? Trade or pensions?

The politicking will be toughest in Michigan, a Democratic stronghold. Its unemployment rate is already above 6%,

compared with 5% nationwide, and the city of Detroit recently had its debt downgraded again by the big ratings agencies. Although Michigan has lost a quarter of its car jobs since 2001, the sector still accounts for 35% of the state's manufacturing employment, so more job cuts would hurt.

This could damage Democrats in races they had expected to win easily. Debbie Stabenow, the state's junior senator, is a target for the Republicans. The state's governor, Jennifer Granholm, has been one of the Democratic Party's stars; but with her approval ratings down, her re-election in 2006 no longer looks assured. She went to Japan this summer in an effort to drum up investment. She also held a closed-door meeting in November with all 17 of Michigan's congressmen to plot strategy.

A particular bugbear is a push by Congress to force firms with underfunded pension plans, such as the carmakers, to make up their shortfall in order to protect the government-backed Pension Benefits Guaranty Corporation. The industry is worried by a Senate bill that would force junk-rated borrowers, such as Ford and GM, to close their pension gap especially quickly. Ms Stabenow and Carl Levin, Michigan's other Democratic senator, were the only two people to vote against the bill, which now has to be reconciled with a less draconian House version.

The unity the mid-west's politicians have displayed in Washington is missing in local politics. After a lot of squabbling, Ms Granholm and local Republicans patched together a deal last month to give tax incentives to local carmakers. In Ohio, by contrast, it is the Republicans who are under pressure to come up with schemes to help the car firms. They control all the state offices, but are worried about losing both the governorship and a Senate seat this year. In Indiana and Kentucky politicians are also worried—though their economies are less exposed.

Another mid-western politician, Barack Obama, has tried to appear statesmanlike. The fast-rising Democratic senator from Illinois, who does not face re-election until 2010, has introduced a bill that would trade “health care for hybrids”. The idea is that the government would help GM and other car firms relieve the high costs of health care for their workers and retirees—the result of over-generous contracts with the UAW—if the carmakers develop greener cars that burn less petrol.

While the region's politicians bicker over how to divide the blame for their car troubles, help may yet come from an unlikely source: Japan. The Japanese remain wary of an American backlash against their success. In a recent editorial, GM's boss, Rick Wagoner, blamed his firm's problems partly on “unfair trading practices, especially Japan's long-term initiatives to artificially weaken the yen”, and called for a “level playing field”. Toyota, which is considering building yet another factory in the United States, may decide that helping Michigan or Ohio is a wiser choice politically than yet another southern state.

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Miracles

Tears in Sacramento

Jan 5th 2006 | SACRAMENTO
From The Economist print edition

A Marian sighting in a troubled diocese

ON A clear and unseasonably warm Christmas Eve south-east of Sacramento, dozens flocked to see what they believed was a miracle—a statue of the Virgin Mary “weeping” what appeared to be blood. This Marian sighting came months after her image was found on a pre-Katrina New Orleans billboard, before that in a Chicago freeway underpass, and before that in a grilled cheese sandwich that fetched $28,000 on e-Bay. To some, it must be a sign.

At the Vietnamese Catholic Martyrs Church in Sacramento County, red marks on the sides of the statue's eyes first appeared on November 9th. The parish priest washed off what he assumed were stains. Ten days later, they reappeared and the pilgrims and media came. The statue stands outside the church; heavy rains have now rendered the “tears” a mere smudge on the left side of the face, but this has not stopped the devout from bringing flowers, praying, and taking photographs. Some have come from hundreds of miles away.

Historically, apparitions of the Virgin have increased during tumult, such as war. But the Vatican does not rush to authenticate them. In the past two centuries only six sightings have met church standards, and none in the past 70 years. This does not worry Maria Elena Gutierrez, who has stopped to pray in front of the Sacramento statue several times. “There is nothing there that makes me think someone is making it happen,” she says. “If this continues, they really should investigate.” The diocese, however, has said it has no plans to look into the matter.

Across the United States, the Catholic church is still trying to recover from a spate of sex scandals that have left dioceses financially weakened and with dwindling congregations. Just before the end of 2005, the archdiocese of Boston offered a settlement that could total $7.5m for about 100 plaintiffs. And a federal bankruptcy court judge ruled that the archdiocese of Portland, Oregon, could not protect parish property from liquidation to settle lawsuits. In July 2004, Portland became the first Catholic diocese in the United States to file for bankruptcy.

Sacramento has shared in these troubles. In June 2005, the diocese reached a $35m settlement for 34 victims of abuse by ten priests. In anticipation of the settlement, it cut operating expenses last year by 15%, mostly by laying off staff. The Vietnamese Catholic Martyrs Church appears to have had a short upsurge in donations and attendance, even though all services are conducted in Vietnamese. But for the beleaguered Sacramento diocese, the strange phenomenon of the weeping Virgin has brought no extra money, only solace.

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CLASSIC
PERTH 2006

Women hunters

Sisters are killing it for themselves

Jan 5th 2006 | FLORENCE, FOUR PEAKS AND MESA
From The Economist print edition

Good news for feminism, bad news for Bambi and the sweet-and-sour bunny

AP

FELICIA MORALES is an unassuming mother of three without an obviously bloodthirsty air. But put a rifle in her hands and something changes. Out in the desert 30 miles south of Mesa, Arizona, she carts a bloody jack rabbit and a dozen dead quail from the bushes with a grin. “My shot isn't bad,” she says modestly. The same goes for Janice Brooks, a former English teacher. She shot an antelope with her Remington at 300 metres—a feat her husband, no mean marksman, confesses he might not have tried.

Over the past 50 years hunting, as Americans call game shooting, has generally been in decline, as the television remote control has lured people away from outdoor pursuits. But the number of women hunters has surged.

According to the National Shooting Sports Federation, some 2.4m American women of all ages hunted in 2004, compared with 2m in 1997; the number taking part in shotgun sports was up 11%, to 1.3m. Another survey (commissioned by the National Wild Turkey Federation) claims that 95% of women approve of women going hunting and 15% have owned a hunting licence.

Most western states, with their open spaces and outdoorsy culture, report a growing wave of interest. Arizona is typical. Gun shops and hunting stores in Phoenix, Glendale and Mesa are seeing record numbers of female customers. Ranges also report plenty of trade from them. Every Thursday the Ben Avery range, the largest in the country, hosts “the Annie Oakley Sure Shots”, a consistently packed free shooting class for women. At the Phoenix branch of the Sportsman's Warehouse, Bob Buffa has to cap his occasional workshop for female shooters at 20 students but says 100 or so sometimes apply.

This being America, the government is trying to help blood sports rather than ban them. The Arizona Wildlife Federation conducts a “Becoming an Outdoor Woman” course twice a year near Prescott. And the state's game-and-fish department also holds workshops: one, at Florence, teaches families hunting tricks and then how to cook dishes such as “No fail Quail” and “Sweet-and-sour Bunny”.

Hunting offers a chance to stock the family freezer. But it is still an expensive sport. Ms Morales's hunt is her sixth in 2005; but with the costs of licences, ammunition, camouflage gear and petrol all going up, she will hunt less in 2006.

Although one reason often given by women for taking up the sport is a chance to bond with men, many women complain about sexism. Novices say that male instructors make them feel stupid; experienced shots say men feel emasculated when a woman out-shoots them. When Ms Brooks, the hotshot former schoolteacher, goes target-shooting, the men alongside often walk away.

Yet most people reckon that women's interest in shooting sports and hunting will continue to grow. One reason is the issue of personal safety. Ms Brooks, who narrowly escaped a vicious attack in 1990, clips a Keltec 32-calibre semiautomatic under her jeans and holsters a Model 19 Glock. She now teaches other women how to shoot (her logo is a dove with a shield). “Women hunt just as well as men and the scarier the world gets, the more women are going to take protection in their hands.”

The broader reason why women may be flocking to hunting and shooting (and you might want to stop reading here if you live in Islington or on the Upper West Side) is, well, it can be fun. Your unbloodthirsty correspondent, having undergone a crash-course in firing a LadySmith and a 9mm Glock, actually managed to hit an (inanimate) target after just 12 rounds and must confess to an adrenalin rush that lasted for hours. This year, she's hunting dove.

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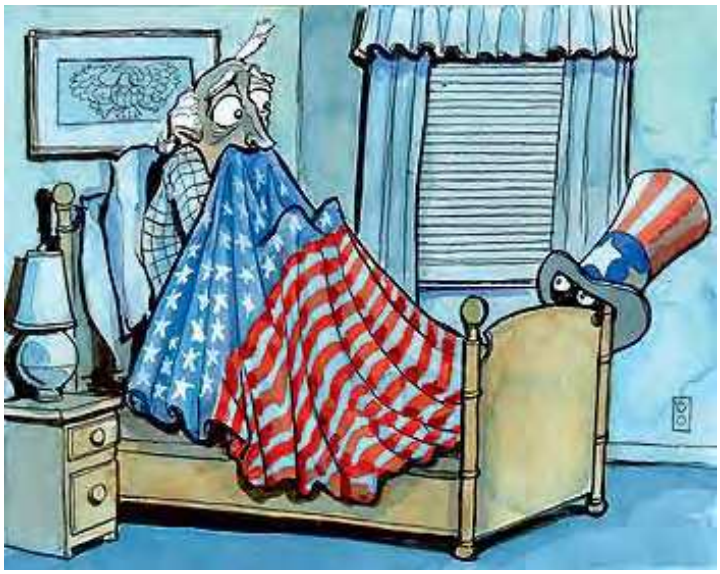
Lexington

The paranoid style in American politics

Jan 5th 2006
From The Economist print edition



It's back, updated for a new generation

RICHARD HOFSTADTER'S classic essay, “The Paranoid Style in American Politics”, was aimed at the American right (it was published in November 1964 in the wake of the Goldwater insurgency). But it is hard to read it these days without first thinking of the other side of the political divide.

Hofstadter argued that the “paranoid style” expresses itself in three habits: “heated exaggeration”, “suspiciousness” and “conspiratorial fantasy”. Victims of the paranoid style have attacked shifting groups throughout American history—from international bankers to freemasons, from the Illuminati to effete liberals—but today they are targeting the White House.

Begin with the fuss over wiretapping. According to Robert Byrd, a Democratic senator from West Virginia, George Bush has assumed “unchecked power” that is “reserved only for kings and potentates”. Barbara Boxer of California says there is “no excuse” for Mr Bush's actions. A growing chorus of outrage, including Congressman John Lewis and John Dean (of Watergate fame), has suggested impeachment. Over at the *Nation*, Jonathan Schell argues that “Bush's abuses of presidential power are the most extensive in American history”. The administration “is not a dictatorship”, he concedes, before adding that “it does manifest the characteristics of one in embryonic form.”

And the proof of dictatorship? On more than 30 different occasions, Mr Bush authorised the tapping of telephone calls made by American citizens. Tapping domestic telephone calls without getting a warrant is illegal. But Mr Bush claims that his constitutional powers as commander-in-chief allowed him to do so because all these calls were international ones. He maintains that going to the courts would have been cumbersome and that his first priority was to prevent another terrorist attack.

You can pick at this reasoning—for instance, there are retrospective warrants that might have done the trick. But it is hard to claim that Mr Bush is being outlandish on any of these scores. John Schmidt, an associate attorney-general under Bill Clinton, thinks Mr Bush has the constitutional power to approve such taps; General Michael Hayden, the deputy director of national intelligence, has argued that the programme “has been successful in detecting and preventing attacks inside the United States”.

That assertion is for Congress to probe, but the real argument here is surely one of nuance: it has to do with how much freedom you should reasonably curtail in the name of security. Mr Bush may have crossed a line, but he has hardly smashed through it. Most European countries have more intrusive surveillance regimes than America's. As for impeachment, the prospect of having to defend Mr Bush against the charge that he went a tad too far trying to avert a terrorist attack is the sort of thing Karl Rove salivates about.

Moreover, the paranoid style is finding an ever larger home in popular culture. In 2004, American cinema-goers trooped off to see Michael Moore's “Fahrenheit 9/11”, a fearless exposé of the hidden forces behind the war on terrorism, and an update of “The Manchurian Candidate”, the quintessential paranoid film. Now they are crowding to “Syriana”, an analysis of American policy in the Middle East, featuring George Clooney. The villains vary: “Fahrenheit 9/11” went for the Carlyle Group, the Saudi royal family and virtually anybody who had met Mr Bush; “The Manchurian Candidate” attacked big business; “Syriana” dislikes oil firms and the CIA. But they all agree that America is run by a sinister cabal that will stop at nothing.

Paranoid optimism

In one way, paranoia is one of America's great strengths—part of its long-standing suspicion of government. America was born in a revolution against George III's tyranny. Hostility towards central government has been a constant of American history. Most periods of heightened executive power during wartime have been followed by sharp reactions. Abraham Lincoln, who suspended *habeas corpus*, was accused of dictatorship and his Republican Party lost seats in 1862; Richard Nixon's abuses of power spawned a host of reforms, including the wiretapping-oversight system that Mr Bush has tangled with.

But there is something less healthy at work on both the left and the right. Hofstadter argued that the politics of paranoia is fuelled by a sense of dispossession—by fury at your loss of relative power to rising groups. In the 1960s, the right was driven by a sense that it was being eclipsed by cosmopolitans and intellectuals. Now the left thinks it is losing power to businessmen and suburbanites. It cannot believe that the north-east—the vortex of civilised America—is losing influence to the South and the West, to people who believe in God and guns, to Mr Bush.

That does not let the president off the hook. Put simply, a man who claimed he would unite the country has given his enemies far too much to be paranoid about. There may well be a case for wire-tapping people in contact with al-Qaeda; but what about refusing to reveal who is on the energy task-force, let alone the (possibly legal but ghastly) treatment of inmates at Guantánamo? There may be a case for asking people to rally around the flag at a time of war; but how does that square with Mr Bush using terrorism to divide his opponents and advance his party's political interests, as he did in 2002 and 2004?

Hofstadter argued that the paranoid style “has more to do with the way in which ideas are believed than with the truth or falsity of their content”. The problem for America's left is not the lack of justified complaints about Mr Bush. It is that their paranoid style—with its propensity to exaggeration and conspiracy-mongering and its inability to distinguish between justified complaints and hysteria—means that their cries are seldom listened to except by people who suffer from the same affliction. Which is sometimes a pity.

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CLASSIC
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Colombia

One and a half steps forward, one back

Jan 5th 2006 | BOGOTÁ
From The Economist print edition

AFP

Less violent, but still far from the unchallenged rule of law

IN AN election in May, Álvaro Uribe will seek a second four-year term as Colombia's president. His claim is a simple one: his tough security policies have transformed the mood of a country racked by the violence of three illegal armies, and made it safer. Many Colombians seem to agree: Mr Uribe's approval rating in the opinion polls stands at 70%. They suggest he may win 55% of the vote in the election. Yet progress in Colombia is never easy. As the year began, Mr Uribe's government faced a setback on one front, disappointments on another, and a small breakthrough on a third.

The setback was inflicted by the guerrillas of Revolutionary Armed Forces of Colombia (FARC). On December 27th, some 300 of them killed 29 soldiers in the group's deadliest attack since Mr Uribe came to power. The soldiers had been guarding workmen eradicating coca—the raw material for cocaine—in La Macarena, a national park. In response, Mr Uribe ordered more eradication squads and troops into the park, and vowed to eliminate all the coca there. Days later the FARC rejected an offer by the government to talk about an exchange of prisoners. The FARC holds scores of hostages, including Ingrid Betancourt, a politician with dual French and Colombian nationality. “With Uribe there will be no exchange,” said the FARC.

The disappointments concerned a messy peace arrangement under which the 20,000-strong right-wing paramilitaries of the United Self-Defence Forces of Colombia (AUC) were supposed to lay down their arms by the end of December. Only 14,000 have done so, and the deadline has been extended to February 15th. The big doubt is whether the paramilitaries will really disband, or will intimidate their way into politics, a fear voiced by the American ambassador last month.

The paramilitaries are notorious for two things: massacres of civilians they consider sympathetic to the guerrillas, and their close links with the cocaine trade. Demobilisation has not been straightforward. The AUC's chiefs worry that Mr Uribe will extradite them to the United States to face drug charges, although the government has tacitly agreed not to. Talks stalled in October after one of them, Diego Fernando Murillo (aka “Don Berna”), was arrested, accused of ordering the murder of a politician. Only in mid-December did the largest AUC grouping, the Central

Bolívar Block, begin to demobilise when its leader, Iván Roberto Duque (aka “Ernesto Báez”), and 2,000 others handed over their guns. This group controls much of Colombia's coca crop. The other AUC groups are also heavily involved in drugs.

Under a controversial law passed last year, nearly all the paramilitaries will be given an amnesty. Prosecutors were supposed to vet all the demobilised fighters, and bring charges against any leaders accused of serious crimes. In practice, little has happened, partly because the government did not issue the necessary regulations until December 30th.

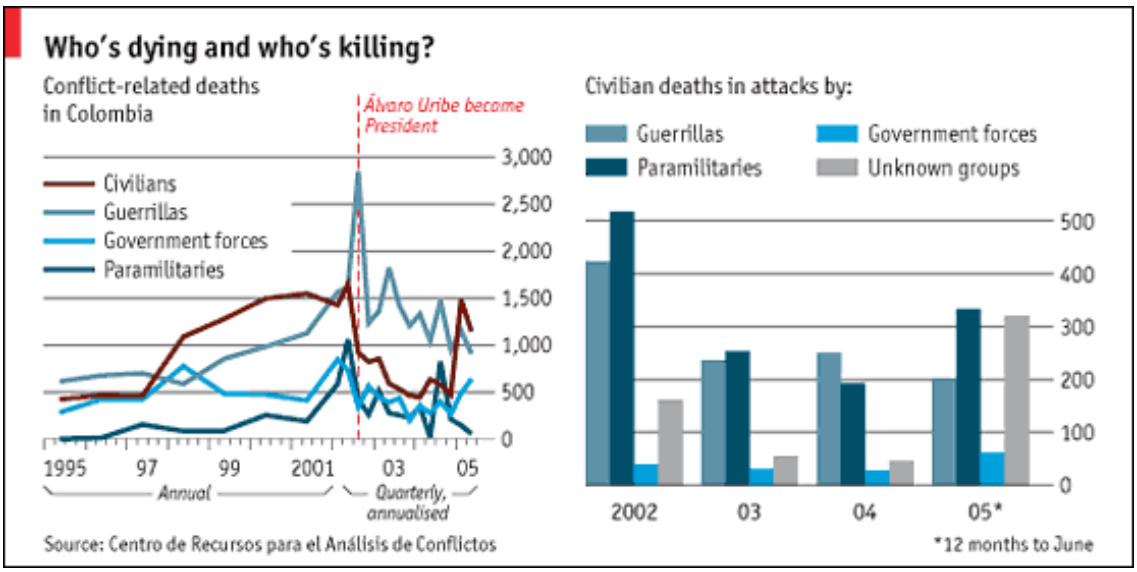
Those paramilitary leaders who were supposed to be confined to a safe part of the country while their legal position was clarified appear to be roaming free. Prosecutors have not yet made much progress in seizing their ill-gotten assets. Many Colombians fear that the paramilitaries will use intimidation and bribery to influence the congressional election due in March. Two of their leaders have boasted that the AUC controls 30% of the existing Congress.

The government's peace commissioner recently admitted that a programme to help paramilitaries into civilian life had been inadequate. Only 460 have been given jobs. The interior ministry reports that 123 former fighters have been killed and 223 have been arrested for such activities as extortion and robbery.

Improvised though it has been, officials argue that getting the paramilitaries to demobilise is an essential step towards ending the fighting in Colombia. A conflict “with 30 years of roots doesn't end with a decree,” says Eduardo Pizarro, a political scientist who heads an official reconciliation commission. “It's not going to be paradise. We are going to have a continuation of crime. But that's normal.”

Better news for the government is that the National Liberation Army (ELN), the smaller of the two leftist groups, with some 3,000 guerrillas, has agreed to start formal peace negotiations after exploratory talks in Havana last month. Officials want to apply the same legal framework to the ELN as it has to the paramilitaries. It is not clear whether the ELN will accept.

Mr Uribe can point to a sharp fall in violence since he took office. The murder rate in Colombia last year fell to its lowest level in two decades. Kidnappings have also dropped sharply over the past few years. Even so, some trends are worrying.



Researchers at CERAC, a think-tank in Bogotá, who have compiled detailed data on the conflict, say killings of civilians by paramilitaries rose in the first six months of last year—despite the peace process (see chart). They reckon that the AUC was responsible for many of the killings whose perpetrators were officially unknown. These were no longer large-scale massacres, but individual murders. Mainly as a result, CERAC (whose findings are available at www.cerac.org.co) reckons that only about 10% fewer civilians were killed in the conflict in the first half of last year than in the six months before Mr Uribe took power. But they stress that conflict-related deaths amount to no more than 15% of all murders in Colombia—a much lower figure than some human-rights groups claim.

Despite last month's FARC attack, CERAC found little evidence of a sustained guerrilla resurgence, but notes that conflict continues across wide areas of rural Colombia. If he gets a second term, Mr Uribe still has much work to do to consolidate the improvement in security that was the main achievement of his first term.

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CLASSIC
PERTH 2006

Haiti

Electoral mirage

Jan 5th 2006 | MIAMI
From The Economist print edition

A new start proves elusive

Get article background

EVER since the United Nations went into Haiti in 2004 in the wake of American and French troops, its main aim has been to organise an election for a new government in the poorest country of the Americas. After three postponements, this was supposed to happen on January 8th. But late last month officials announced yet another delay—an indefinite one. Some Haitians now doubt whether the vote will give their country the new start it needs.

Officials at Haiti's electoral council blame the delays on foreign incompetence. Their international counterparts insist that too much hangs on the contest for it to be rushed. Over 80% of the 4m eligible Haitians are registered as voters. But many identification cards have yet to be distributed. Equipment and training are lacking at some of the voting centres.

Aid worth more than $70m has already been spent on organising the election. Some Haitians worry that too little has been spent on political reconciliation since the violent overthrow of the former president, Jean-Bertrand Aristide, in 2004. The country's divisions are reflected in the 54 candidates who aspire to one of the world's tougher jobs.

Two of the more popular aspirants have been disqualified. One of them, Dumarsais Siméus, is a leading black businessman in the United States. He was barred because he holds dual nationality and has not lived in Haiti for the required five years before the vote. He is challenging this ruling in court. Gérard Jean-Juste, a radical priest (as Mr Aristide once was), is in jail on charges his supporters consider trumped up.

Mr Aristide's party is split. Its largely exiled leadership is boycotting the election. A candidate from one faction trails in the polls. Many of Mr Aristide's supporters favour René Préval, once a close ally and himself a former president. Mr Préval says privately that he now wants nothing to do with Mr Aristide. If Mr Siméus is excluded, his votes may go to Mr Préval, perhaps giving him an outright victory. Haiti's businessmen might feel that their revolt against Mr Aristide had been in vain. But at least the election would have resulted in a clear mandate—when, or if, it takes place.

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Peru and Chile

Fujimori's trials

Jan 5th 2006 | LIMA AND SANTIAGO
From The Economist print edition

An extradition test for Chile's courts

AFP

Wanted in Peru

WHEN he left his refuge in Japan in November and flew to Chile in a private jet, Alberto Fujimori, Peru's strongman president from 1990 to 2000, took a gamble. Although an international warrant had been issued for his arrest on charges of human-rights abuses and corruption, his advisers expected he would face no more than a brief period of house arrest in Chile. From there he planned to orchestrate a campaign to get his name on the ballot for a presidential election in April—or at least get supporters elected to Peru's Congress.

The gamble quickly came unstuck. At the urging of Peru's government, Mr Fujimori was locked up at a prison-officers' training-school, where he now has limited access to visitors and cannot tape his programme for two Peruvian radio stations or update his web page. How long he will stay there will be settled in the next few weeks. On January 3rd, Antonio Maldonado, a Peruvian anti-corruption prosecutor, delivered an extradition request, backed by 10,000 pages of evidence. Along with these came a plea to deny Mr Fujimori bail while his extradition case is considered, which will be many months.

Chile prides itself on applying the rule of law more rigorously than its neighbours. Its courts do not lightly extradite: they have approved just ten of 38 requests over the past decade, says Mr Maldonado. Among those who have escaped extradition are Carlos Menem, a former president of Argentina, and Eduardo Calmell del Solar, a Peruvian newspaper owner accused of taking bribes from Vladimiro Montesinos, Mr Fujimori's corrupt spy chief.

Chile and Peru signed an extradition treaty in 1932. But to get his man, Mr Maldonado must offer evidence against Mr Fujimori sufficient to justify his indictment under Chilean law for a serious crime that was not political.

In Mr Calmell del Solar's case, Chile's Supreme Court ruled that the charges did not amount to a crime under Chilean law. The case against Mr Fujimori is weightier—and Peru's prosecutors have done more homework. The most serious charges involve the murders of 15 people at a barbecue in Lima and of ten people from a teacher-training college in the early 1990s during a “dirty war” against the Shining Path terrorist group. The murders were the work of an army death-squad, whose operations Mr Fujimori is accused of knowing about and doing nothing to stop. He is also accused of giving a $15m pay-off to Mr Montesinos, authorising illegal phone tapping, bribing opposition legislators and stealing Japanese donations intended for Peru's poor.

Mr Fujimori may have expected similar treatment to Mr Menem's. But the Argentine faced only corruption charges, and of lesser magnitude. On Mr Fujimori's watch, Mr Montesinos organised a vast web of bribery and extortion. It may also be relevant that Chile's courts are currently trying General Augusto Pinochet for allowing death-squads—and Chile's government pressed Britain to extradite the former dictator after he was arrested in London in 1998. In Mr Fujimori's case, “any reasonable judge should reach the conclusion that there are grounds for extradition,” says José Miguel Vivanco, a Chilean lawyer at Human Rights Watch in New York.

Ever since Chile grabbed a chunk of Peru in a 19th-century war, relations between the two countries have been marked by mistrust. But Chile's government, which by law cannot intervene in extradition cases, would doubtless be embarrassed for the country to become a haven for political scoundrels.

Whatever the outcome, the former president may have lost his main battle. Last year, Peru's opinion polls put him

at or near the head of a crowded field for the election. But protests against his arrest have fizzled. The polls give a surrogate candidate, Martha Chávez, only 1%, and show that support for his party's congressional candidates has dropped to around 6%. Peru's voters are notoriously fickle. But it seems that, like so many authoritarian rulers before him, Mr Fujimori may have made the mistake of believing in his own invincibility.

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PERTH 2006

Canada's election

So far, so good for Harper

Jan 5th 2006 | OTTAWA
From The Economist print edition

A strong start from the Conservatives

PREOCCUPIED with Christmas, Canadians shrugged off the first five weeks of a two-month campaign for an unseasonable federal election on January 23rd. Yet during this phoney war Stephen Harper, the leader of the Conservative opposition, has quietly gained ground on Paul Martin, whose Liberal minority government was defeated in a confidence motion in Parliament in November.

Several opinion polls show the two main parties within a point or two of each other, with the Conservatives holding a narrow lead in Ontario, the most populous province. That would point to another minority government—but one that might be led by Mr Harper.

The Conservative leader has closed the gap through a combination of clever tactics and luck. The Liberals stuffed a number of promises into a mini-budget announced days before the confidence vote. Mr Harper has since hogged the headlines with daily promises of his own.

He has done his best to prevent the Liberals from painting him as an austere social conservative, as they did successfully at the last election, in June 2004. But his promise to be tough on crime has chimed with a panic over a rash of murders, including a shoot-out on Toronto's main shopping street after Christmas that killed a 15-year-old girl.

On some issues, Mr Harper has abandoned conservative principles to march to the centre. For example, the Conservatives want child-care support for all, whereas Mr Martin argues that it should be concentrated on poorer families. This policy difference prompted a gaffe from Scott Reid, Mr Martin's spokesman, when he mocked a Conservative plan to give C$1,200 ($1,040) a year to parents of every pre-school child, saying it would be spent on “beer and popcorn”.

The Liberals have made other mistakes. The police are investigating insider trading after the leaking of a statement to be made by Ralph Goodale, the finance minister, that he would not tax investment funds known as income trusts. Mr Goodale is not himself under investigation. But his refusal to resign over the affair has allowed Mr Harper to revive claims of Liberal sleaze, such as the siphoning of money from an earlier government campaign to promote federalism in Quebec.

With the election so finely balanced, the final debates among the party leaders on January 9th and 10th may be decisive. The polls suggest most voters want change of some sort. So far, at least, Mr Harper, who is 20 years younger than the prime minister, has done his best to offer one.

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Zero hour in Mexico

Jan 5th 2006
From The Economist print edition

A Latin American revolutionary sets off on a motorcycle for a lengthy tour. Yes, the resemblance to Ernesto “Che” Guevara was intentional when Sub-Comandante Marcos, the leader of Mexico's Zapatistas, began a six-month motorbike tour of the country, his trademark ski-mask topped by a reflective helmet. But if history is repeating itself, it is as a footnote—the revolutionary as poseur. Like Guevara, Mr Marcos has long showed a flair for public relations. He launched his jaunt to promote indigenous rights in front of several thousand supporters on New Year's Day, the 12th anniversary of the brief Zapatista rising in the poor southern state of Chiapas. Saying he is no longer a military leader, he has rebranded himself as “Delegate Zero”. He calls the tour “the other campaign”, referring to a presidential election in July. In contrast to 1994, Mexico is now a democracy. Mr Marcos may excite anti-globalisers in rich countries but most Mexicans seem bored. *Reforma*, a centrist newspaper, captioned its picture of the man on a motorcycle: “Did somebody order a pizza? No, it's Marcos!” On day two of the tour, Delegate Zero switched to a car.

Reuters

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Greying Japan

The downturn

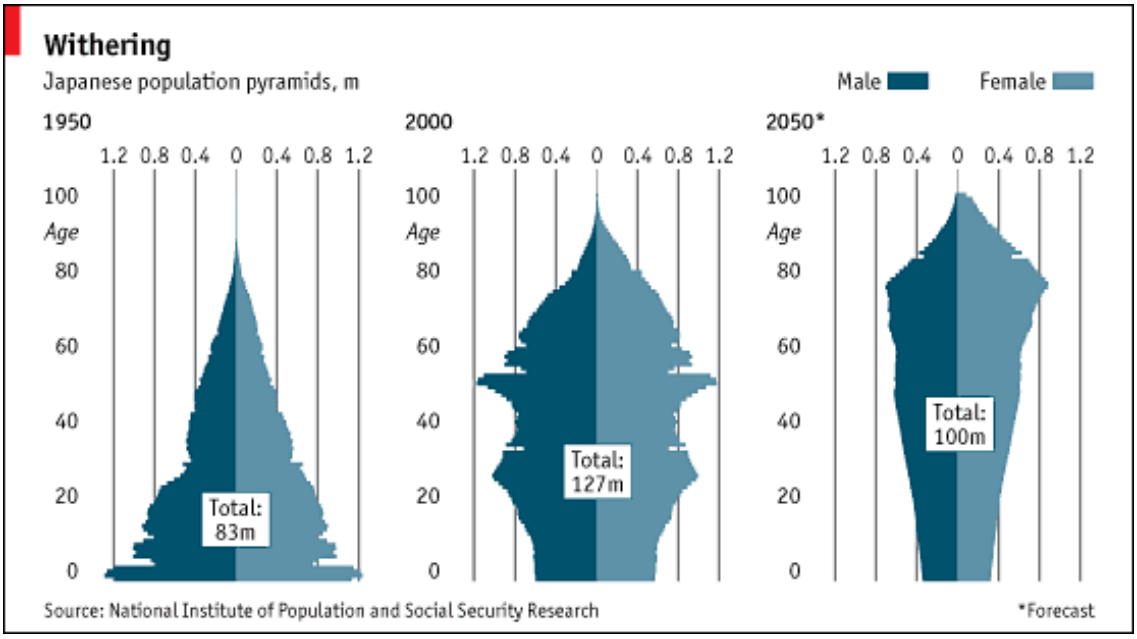
Jan 5th 2006 | TOKYO
From The Economist print edition

But ageing employees need not be a problem, if companies adjust

JAPAN'S population is in decline. As of last October 1st, the government announced last week, giving the results of its latest five-yearly census, Japan's 127m-odd population was 19,000 fewer than a year earlier. Deaths had outstripped births for the first time in a period of peace since records have been kept. A falling population, the *Yomiuri Shimbun* duly wailed, meant that national survival was at stake. It may have a point: with no change in the current fertility rate—below 1.3 children per woman of child-bearing age—the last Japanese will die as soon as 2800.

Such are the perils of extrapolation. The more immediate demographic issue, though, is not so much the predicted fall in Japan's population, to as low as 100m in 2050, some say, but rather a shift in its composition. For as well as a low birth rate, life expectancy continues to lengthen (if that were not so, Japan's population would have started to fall some time ago).

Japan is greying at an unprecedented rate. Half a century ago, the proportion of the population over 65 stood at around 5%, well below that in America, Britain, France or Germany. Today, Japan's proportion of elderly, at 19%, is the highest in the world, and is forecast to reach almost 30% by 2025. In particular, an exceptionally large group of Japanese, the baby-boom generation, is making its way towards retirement. After the second world war, returning Japanese soldiers married, settled down and produced children in large numbers. Between 1947 and 1949, an average of 2.7m children were born a year (with another 2.3m in 1950). That was 30-40% more than in the succeeding years. It made for a more defined population pyramid than, say, America, where the baby-boomers were born over several more years. Today, the country's demographic profile looks something like a Japanese lantern. Soon, it will look more like a narrow-based urn (see chart).



From next year, the baby-boomers start to retire (60 being the minimum mandatory retirement age for now). The prospect is causing some anguish among policymakers. As youngsters, these people were the shock troops during the golden period of Japan's post-war economic transformation. Today, they are the custodians of years of accumulated technical and management skills. Their absence, some suggest, will lead to a shortage of skilled workers and mentors, a loss of productivity and even a surplus of office space. *Mama-san* in her bar in Ginza will miss this lot.

A less noticed aspect of the greying of Japan is the coming sharp decline in the population of the youngest workers. At present, some 16m Japanese are in their 20s, many of them children of baby-boomer parents. But the number in this age bracket will shrink by about 3m over the next decade. The consequence of all this is, first, that fewer workers will support an ever growing number of non-workers, other things being equal; and, second, that the demographic shape of the workforce is assuming that of an inverted pyramid, with fewer young workers at the base where once there were many. These factors combined lead some commentators to speak of dire consequences: of a national malaise led by a decline in living and even educational standards (soon, for instance, you will be able to gain a place at university simply by sitting the exam), accompanied by a government bankrupted by retirement obligations.

Yet this is all far from inevitable. Atsushi Seike, a labour economist at Keio University, argues that, since the great bulk of older workers are company employees, the solution lies in fixing the corporate employment and retirement systems to allow people more easily to work for longer. Those systems were designed for the age of the pyramid. When lots of young people were coming into the workforce, mandatory retirement was adopted by companies who wanted to make room for them. The policy was also useful for getting rid of surplus workers that employment-protection laws otherwise stopped from being laid off. As a result, nine-tenths of companies with more than 30 employees today set a mandatory retirement age, usually 60, the legal minimum.

The government and some companies are starting to respond to the new circumstances. Already, eligibility for the fixed part of the state's two-tier pension benefit has been raised to 62; it will be 65 by 2013. Eligibility for the bigger, earnings-related part still stands at 60 till 2013, but rises to 65 by 2025. To bring corporate practices into line, a law passed in 2004 takes effect in April requiring companies to raise the minimum mandatory retirement age to 65 by 2013—or, if that is not feasible, to provide employment until they are eligible for the fixed part of the state pension.

These adjustments, Mr Seike thinks, are just tinkering at the edges of an outdated system. Since life expectancy has leapt by nearly 30 years since the war, to 82 on average, then the minimum age for pensions should be raised swiftly at least to 67 and preferably to 70. Moreover, he believes, mandatory retirement—forcing people to stop when they are keen to work longer and capable of doing so—"has no place in a society that hopes to make full use of its older citizens." It should be scrapped altogether. So should age discrimination in hiring: many job advertisements are closed to anyone over 45.

Certainly, most older Japanese want to work. Indeed, the average working man finally leaves the labour market when he is approaching 70. The problem is that he is given jobs that do not always match his abilities. A system of pay based on seniority rather than merit, which once ensured employee loyalty, now imposes a financial burden on companies, making them unwilling to keep even good workers in their former jobs. So getting rid of mandatory retirement would also put welcome pressure on companies to revise pay scales better to reflect ability rather than

length of service. That, surely, would suit ambitious younger people too.

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India's opposition

Passing the torch

Jan 5th 2006 | DELHI
From The Economist print edition

But to whom? And when?

AP

Vajpayee goes; Advani stays

THE leadership and policy squabble that has enveloped India's Hindu-nationalist Bharatiya Janata Party (BJP) since it unexpectedly lost a general election 19 months ago shows no signs of abating. Efforts at the party's 25th anniversary conference at the end of December to replace its two elderly top leaders with people in their mid-50s failed to eliminate any of the contenders. Instead, the list of rivals grew longer.

Atal Behari Vajpayee, the 81-year-old former prime minister and the country's favourite BJP politician, announced that he would not stand again in a parliamentary election. But he immediately gave himself a continuing role as king-maker by boosting the standing of Pramod Mahajan, the party's general secretary and one of the more controversial mid-50s hopefuls. And while Lal Krishna Advani, who for more than 30 years had been Mr Vajpayee's hard-line colleague, reluctantly stepped down as party president, he confirmed that he would remain leader of the opposition in parliament and saw himself as a prime ministerial candidate for the next general election—even though it is not due till 2009, when he in turn will be 81.

Mr Advani's successor as party president is Rajnath Singh, 54, a capable administrator who has held senior posts in the central government and in the state of Uttar Pradesh, and wants to focus the party's economic policies on rural development, which it neglected in the past. But he was chosen merely as the least unacceptable candidate, and will have a tough job maintaining his post beyond an initial year.

“The BJP is passing through a crisis,” says Mr Mahajan, referring to the leadership muddle and post-election problems that culminated in a blistering row last June. That is when Mr Advani made what the party and its parent organisation, the Rashtriya Swayamsevak Sangh (RSS), saw as shockingly over-generous remarks about Mohammed Ali Jinnah, the founder of Pakistan, India's great rival. The crisis has since reduced the BJP's effectiveness as a parliamentary opposition and drawn attention to a split within the Sangh Parivar (the Hindu “family of organisations” that clusters around the RSS) over whether the BJP should revert to the strong *Hindutva* (“Hinduness”) policies that Mr Advani used to espouse, or move to a position nearer the centre of Indian politics.

Most of the youngish hopefuls would probably support a more centrist position. They favour policies that concentrate on younger peoples' priorities, such as reforming the economy, rather than the BJP's old *Hindutva* preoccupations such as rebuilding a Hindu temple in the city of Ayodhya. But none of them yet dares say so openly for fear of being damned both by their competitors for stardom and by hardliners. Nor does any of them yet dare to challenge Mr Advani as parliamentary leader, or speak against Mr Singh.

Mr Mahajan currently has a lead over the other hopefuls, following his endorsement on December 29th by Mr Vajpayee. A former communications and parliamentary-affairs minister who has held various party offices and is an effective campaigner, he is the most charismatic of the contenders in his age group. He would probably be the leadership favourite, but for personal controversies that include allegations (which he denies) that he favoured Reliance Infocomm, a telecoms company controlled by the Mumbai-based Ambani family, when he was communications minister. But, along with other hopefuls who include Sushma Swaraj, the BJP's leading female politician, he will have to wait and see how long Mr Advani's currently robust health and more shaky political stamina last—and who the RSS favours. The BJP's long squabble is far from over.

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Afghanistan

A place for warlords to meet

Jan 5th 2006 | KABUL
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A new parliament convenes

EPA

The honourable members

AFTER three weeks in business, Afghanistan's new parliament, the country's first for three decades, oozes goodwill and echoes with calls for national unity. Not bad for a congress of former mujahideen and Taliban commanders, communists, tribal dictators and urban professionals. But how long will it last? And, more pressingly for weary Afghans, what can so incongruous a democratic body achieve?

It is not without men and women of integrity. Besides, its mere existence has made Afghans feel more represented in government. But many are unhappy that the architects of a brutal civil war have, somehow, acquired seats. The big three mujahideen parties, Hizb-e-Islami, Jamiat-e-Islami and Ittihad-e-Islami, are the most powerful in the parliament, over half of whose members are former fighters.

More happily, not all these holy warriors are radical Islamists: only around 50 of the 249 MPs are reckoned to fall under that description, with around the same number thought merely conservative (by Afghanistan's admittedly exacting standards). The rest are moderate mujahideen, royalists, Pushtun and other tribal nationalists, and an assortment of local champions. Maybe 50 members could, at a pinch, be described as secular and progressive, including half-a-dozen moustachioed former communists, survivors from the relatively efficient government left in place by the Soviet Union and overthrown by the mujahideen in 1992. The ethnic balance of the parliament more or less mirrors that of Afghan society, with the largest group, the Pushtun, holding 47% of seats.

There is already discord within this pack. A female MP, Malalai Joya, who had the temerity to rail against the “criminal warlords” in the assembly, has received death threats. Two elected candidates were murdered before the parliament convened. Last month, the government wisely suspended what had become known as the “assassination clause”, which decreed that MPs who die in office should be replaced by the candidate who came second on the original ballot.

With powers to sack ministers and block legislation, the parliament could make life difficult for Hamid Karzai, Afghanistan's president. How he will juggle its various groups is unclear. For four years, he has veered unpredictably between the mujahideen conservative and secular reformist cliques in his government. In the contest to be speaker of parliament, he gave discreet backing to Abdul Rasul Sayyaf, an extreme Islamist accused of revolting war crimes, but a fellow Pushtun. Seemingly, Mr Karzai considered him the only candidate capable of defeating Yunus Qanuni, the self-styled leader of the opposition and a Tajik. If so, he was wrong. Mr Sayyaf's war record pushed a number of Pushtun members to back Mr Qanuni, who defeated his rival and won the contest by

five votes.

A crucial test of the parliament will come later this month when it will vote to approve Mr Karzai's cabinet. Heads are likely to roll, with the mujahideen keen to oust several western-educated, technocratic ministers. This would be popular, tapping into Afghans' universal dissatisfaction with the slow pace of reconstructing their country. A similar target would be international NGOs, which are generally considered inept and wasteful; many MPs say they want foreign aid money to be channelled through government ministries. Fine, but given the corruption there, they would get much less of it.

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Indonesia

Making a list, checking it twice

Jan 5th 2006 | BANGKOK
From The Economist print edition

A return to bombing in Sulawesi

EVERY Christmas, Indonesian Christians' holiday cheer is sadly tempered by fear that they may fall victim to terrorism. On Christmas Eve 2000, Islamic extremists set off bombs at 24 churches around Indonesia, killing 19 people. Every year since then, police and community groups have mounted much-publicised campaigns to thwart potential attacks. Despite these efforts, on December 31st, a bomb killed seven Christians and injured 65 more at a market in Palu, the capital of Central Sulawesi province.

The police have questioned several suspects and detained one, but do not seem sure who the culprits are. Most observers assume that Islamic militants of some sort must be responsible, given the nature of the target. The market in question sold only pork and dog meat, which observant Muslims do not eat, virtually guaranteeing that all the victims would be Christian.

Unlike Indonesia as a whole, with its overwhelming Muslim majority, Central Sulawesi has roughly equal numbers of Christians and Muslims. In 2000 and 2001, widespread fighting broke out between the two communities, claiming perhaps 1,000 lives and displacing tens of thousands. The government brokered a peace accord late in 2001, but since then there has been a string of unexplained attacks on Christians. In May, a bomb in Tentena, a Christian town, killed 22. In October, unidentified assailants decapitated three Christian schoolgirls near the town of Poso.

The police have not got to the bottom of any of these incidents, but the national headquarters in Jakarta did recently send a top detective out to Sulawesi to jolly the investigations along. A recent report by Sidney Jones, of the International Crisis Group, a think-tank, argues that the likeliest perpetrators are radical Muslim veterans of communal strife in Central Sulawesi and the nearby provinces Maluku and North Maluku. At the height of the fighting, radical groups all over Indonesia recruited, trained and despatched volunteers to battle local Christians, who had committed several grisly massacres of their Muslim neighbours. Many of these would-be holy warriors remain in the area to this day, have kept in touch with the network through which they were recruited, and would presumably be keen to rekindle the conflict.

The police recently discovered a camp in Maluku, for example, where militants had trained new recruits. The suspects who led them to the camp were linked to the killing of five policemen in the province in May. Two of the

attackers, it turned out, belonged to a radical group in Central Sulawesi, while others were from Maluku, Java and Sumatra. Several had received training in bomb-making.

Most people in Central Sulawesi, however, seem hearteningly resilient to such provocation. There has been no return to collective violence. The number of people killed in religious strife in Indonesia in general has fallen from a high of almost 3,000 in 1999 to a few dozen in recent years. Both Muslim and Christian leaders now routinely condemn attacks, and call for restraint. Events that could have heightened communal tensions, such as local elections last year, passed without incident.

If anything, the biggest risk is that outsiders might forget about the potential for conflict. Aid agencies' attention shifted to Aceh province after the tsunami there in 2004, reducing funding for reconstruction and development projects in Central Sulawesi. Several NGOs have recently halted operations in the province altogether. Perhaps the latest bombing, one observer muses, will prompt them to reconsider.

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China

Dragonhead dreams

Jan 5th 2006 | ZHENGDONG
From The Economist print edition

Optimism on a grand scale

IN CHINA'S central plain a big new city is being built. The towering half-finished buildings of its central business district encircle an artificial lake and an exhibition centre that will be one of China's biggest when it opens later this year. Plans are afoot for a hexagonal pyramid-shaped hotel that would be nearly as tall as the Eiffel Tower. Broad highways are spreading across former farmland. But will the people come?

Zhengdong New District is rising from what used to be a military airfield surrounded by fields, fishponds, factories and scrapyards east of Zhengzhou, the capital of Henan province. Though called merely a district, its planned area is about the same as that of Zhengzhou itself, and its projected population of 1.5m will almost rival that of the adjoining city (population 2.3m). It is a project as ambitious as Shanghai's Pudong area, which in less than 15 years has been transformed from semi-rural expanse into China's futuristic financial capital. Yet Zhengdong New District is more than 500km (300 miles) from the sea, in the backward hinterland.

Zhengzhou officials like to compare the project to Pudong, which helped restore Shanghai to glittering greatness after decades of stagnation. Just as Shanghai has become known as the “dragonhead” of an industrial boom in the Yangzi river delta, Zhengzhou's leaders see their city—helped by Zhengdong New District—as the dragonhead in what China dubs “the rise of the central area”, a hoped-for economic take-off of its poorer inland provinces. Zhengdong is due for completion in 2015 at a cost, according to one local state-owned newspaper, of some $25 billion.

Given the scale of the Zhengdong plan, it is striking that China's national press has said little about it. This may be a sign that officials in Beijing are reserving judgment. The project won no special dispensation during a central-government campaign in 2004 to cool a nationwide frenzy of property development, and came to a halt for several months. But the construction workers are now back out in force.

Zhengzhou officials are certainly out to impress. After unveiling their idea to build Zhengdong in 2001, they hired a renowned Japanese architect, Kisho Kurokawa, to design the new district and its main showcase buildings, complete with business, residential, high-tech, university and industrial zones, an exhibition centre and two artificial lakes. But the city has had to tame its ambitions somewhat. It had hoped that the glass hotel by the business district's lake would be 360 metres (1,170 feet) tall, close to the height of Kuala Lumpur's Petronas Twin Towers (375 metres, without masts). But it failed to get permission for this, so the design has been scaled back to a still impressive 280 metres, about the height of the Trump World Tower in New York. It will cost $230m. Though there is uncertainty as to where all the money is coming from, China has confounded critics before. The former fishing village of Shenzhen next to Hong Kong has become one of the country's wealthiest cities. Pudong's skyline is a magnet for foreign businesses. Zhengzhou lies on major transport arteries, and is home to the country's biggest grain wholesale market. Henan, with 97m people, is China's most populous province. And the Zhengdong project has a degree of political impetus, being a pet project of Li Keqiang, a former party chief of Henan (now of Liaoning province in the north-east), a rising young star of Chinese politics with a doctorate in economics.

But Zhengdong has competition. Since March 2004, when the prime minister, Wen Jiabao, called for “the rise of the central area”, the big industrial city of Wuhan, capital of Hubei province to the south, has also been vying for “dragonhead” status. Inter-city rivalry in China, combined with the public's inability to scrutinise government spending, often leads to great waste.

One former Zhengzhou official says he fears the artificial lakes and canals of Zhengdong will drain the city's meagre water supplies. “Shanghai and Zhengzhou are not the same. Shanghai discusses projects first. Zhengzhou just builds them, even though they end up completely empty,” he says. As the *China Business Guide*, a Hong Kong publication, puts it, Zhengdong is either “a vision of the future or the height of folly”. The city's leaders appear

unperturbed.

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Israel and Palestine

What comes next?

Jan 5th 2006 | JERUSALEM
From The Economist print edition

Reuters

With Israel's prime minister gone from the political landscape, who will now set the agenda for the Middle East?

ONE can only imagine what was going through the minds of the surgeons who operated on Ariel Sharon through the night of January 4th. As *The Economist* went to press, they had managed to stem massive haemorrhaging in the Israeli prime minister's skull after his second, and much more serious, stroke in three weeks. Even so, his condition is still described as “severe”.

Even if he recovers and returns to work, and there are only slim chances of that now, nobody would rely on his staying healthy for long. And that means bidding farewell to the man who has led Israel for the past five years, longer than any other recent prime minister; the man whom many Israelis of both right and left—even those who reviled him as one of the chief architects of Israel's greatest folly, its programme of settlement-building—had come to see as the only politician capable of leading the country in any direction.

His departure redraws a political map that has already been torn up twice since he pulled Israel's troops and settlers out of the Gaza strip in the summer: first when Amir Peretz re-energised the moribund Labour Party by beating the veteran Shimon Peres for the leadership, and then when Mr Sharon himself abandoned the poisonous infighting of his right-wing Likud party to form a centrist one, Kadima (“Forward”). It attracted luminaries from both of the others and its support seems to have grown and grown; on the day Mr Sharon was hospitalised, a newspaper poll gave it 42 seats in the 120-seat Knesset, a bit more than double the projection for Labour and three times that for the Likud.

Without Mr Sharon, however, what is Kadima? Nobody is sure. But if—to over-simplify grossly—Labour stands for negotiating peace with the Palestinians and the rump Likud for holding on to occupied lands regardless, then recent hints suggest that Mr Sharon's policy was eventually to abandon the international “road map” peace plan by dismantling more settlements on the West Bank, but unilaterally and at his own pace.

While paying lip-service to the road map, Mr Sharon has always refused to carry out Israel's side of the agreement (freezing settlements) while not helping, and some would say undermining, the Palestinians' efforts to dismantle terrorist groups. The end result might, one day, be a Palestinian state; but a truncated one, possibly dotted with Israeli outposts, its borders under Israeli control and its core city, East Jerusalem, surgically removed.

If that is Mr Sharon's plan, it is working, but only because Mahmoud Abbas, the Palestinian Authority (PA) president, has proved a hopelessly inadequate leader. Recently Gaza has woken daily to new symptoms of the

lawlessness that has reigned there since the Israeli disengagement. There has been a string of kidnappings, mostly by militants loyal to the ruling Fatah party trying to extort jobs and other concessions from Mr Abbas. He usually grants them, encouraging the abductions to continue and exacerbating the PA's deepening fiscal crisis.

Lawless in Gaza

Mr Abbas's security services not only cannot cope but, perhaps at the prodding of local bosses, are causing their own insurrections. In the first few days of 2006, police stormed courthouses and the Rafah crossing on the border with Egypt in protest at the killing of one of their own men in a clan shoot-out, forcing the crossing point—a first test of the PA's ability to run its own borders—to close briefly. On January 4th non-Fatah militants responded to the arrest of one of their men by breaching the border with bulldozers, killing two Egyptian soldiers and allowing hundreds of people to push their way through.

The chaos is partly a by-product of the run-up to PA legislative elections, the first in a decade, due on January 25th. Again, Mr Abbas has managed to mishandle these. He allowed a dispute over candidacies to split Fatah, though the party is fielding a joint list again. Now he says the election may be postponed again, if Israel prevents voters in Jerusalem from taking part. But any poll might be difficult to organise given that the Palestinian elections commission resigned on January 5th in protest at interference by Fatah officials.

The optimistic scenario is that a freshly legitimised parliament will lower the political tension; and that Hamas, the Islamist main opposition party, which should win a good many seats, will start to subject its militias to the PA's control and eventually adopt a more pragmatic stance towards Israel, as its growing government role makes it more answerable to Palestinian voters. The gloomier view is that the election results will be disputed, new fighting will break out and Mr Abbas will lose the last shreds of control. If that happens, Israel would have every reason to claim that it does not have a partner with whom it can follow the road map.

Israeli politics without Sharon

That might have been Mr Sharon's next move. Who will make it now? Kadima, his new party, has three problems: it has no clear platform, no obvious leader, and contains an unstable mix of ambitious rivals drawn from opposing parties. Ehud Olmert, the acting prime minister and a former mayor of Jerusalem, is experienced, decisive and tough; and he spoke out in favour of replacing the road map with unilateralism even before Mr Sharon announced the Gaza disengagement, so he would probably represent continuity. However, voters dislike him, unless he can somehow cloak himself in Mr Sharon's mantle. Tzipi Livni, the justice minister, is popular across the spectrum for her honesty, but lacks political weight. Mr Peres, having found a new home in Kadima after leaving Labour, has statesmanship but a record as an election-loser.

Kadima's mix of former Labour and Likud members will struggle to choose a leader who balances electability, competence and their own old loyalties. A lesser-known compromise candidate might be found. But it is hard to see them all uniting behind whoever wins. Some may drift back to their old parties. Kadima might even collapse. Even if not, it is easy to imagine either Labour or the Likud leading the next governing coalition after elections on March 28th (if they are not brought forward), and taking the peace process in its own direction.

For the present, most Israelis have the same curious, suspended-in-mid-air feeling that they had when Mr Peretz won control of Labour and Mr Sharon formed Kadima—when, for a few days, until the polls began to draw the new political landscape, anything was imaginable. As they float, the voters will be much more susceptible to the winds from the Palestinian side. Calm and order there will boost Labour's chances; continued chaos will push the newly hardline Likud to the fore. Mr Abbas now has another window of opportunity, but there is no knowing how long it will stay open. To judge by his past performance, it is hard to see him using it.

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CLASSIC
PERTH 2006

Iraq

The wrong lot won, dammit

Jan 5th 2006
From The Economist print edition

A disputed election may result in an awkward government

SOME time in the next two weeks, the final results of December 15th's election for Iraq's first post-war parliament will be announced. Allegations of fraud have delayed the count, but Iraqi politicians say they can already make a good guess about the balance of power in the new parliament. Projections based on partial, unconfirmed results give the United Iraqi Alliance (UIA), a coalition of Shia Islamists, at least twice as many votes as anyone else—and so 120-130 of the 275 seats. Second place will probably go to a coalition of the two main Kurdish parties, with around 50 seats, and third place to the Sunni Arab Islamist Iraqi Consensus Front, with just over 40. Iyad Allawi, a secular Shia ex-prime minister who many thought could gather votes from anti-clericalists opposed to the UIA, will come in a distant fourth, with perhaps 25 seats. He will be followed by Sunni nationalists, Kurdish Islamists, parties based on smaller ethnic and religious minorities, and others.

This outcome, which means that nearly all Iraqis voted according to ethnic and sectarian divisions, means that the Shias will be almost as dominant in this government as in the last, when the Sunnis boycotted the vote. Although for now all sides are clamouring for a government of national unity, the UIA's strong showing means it can probably exclude any group it pleases, thus burying American and British hopes that the secular parties would break up the UIA and cast hardline Shia doctrine, viewed as a polarising force, out of power.

The Sunnis are not happy. Their leaders, as well as Mr Allawi's supporters, say that the UIA's strong showing in ethnically mixed provinces like Baghdad owes more to gangs of Islamists who stormed into polling stations intimidating opponents, and sometimes demanding to vote several times, than to the real demographic balance. Those challenging the results have organised demonstrations in both the capital and the provinces—one of the first times that Sunni leaders have used street protest to influence politics—calling for a re-run of the election and threatening to boycott the parliament if their demands are not dealt with.

A re-run is almost certainly out of the picture, as both America and the UN have said the election was free and fair enough. The Independent Electoral Commission of Iraq is reviewing results and, in a sop to the Sunnis, has flown in a team of international experts to monitor the handling of the complaints. The commission says it may annul the results from polling stations where egregious offences took place.

That, however, is not likely to alter the outcome. Serious offences almost certainly occurred, but probably not on a scale large enough to shift more than a handful of seats. Most observers feel that the preliminary results more or less reflect the political loyalties of the country. One difficulty stems from the insistence of many Sunnis that their share of Iraq's population is not the 15-20% normally estimated but over half. This attitude makes many Shias inclined to belittle Sunni grievances. If the former ruling minority cannot accept that it will no longer rule a democratic Iraq, they argue, then the only course of action is to ignore them until they do.

However, the Sunnis and Mr Allawi also have better-founded grievances. The electoral commission could have done much more to inspire confidence in its ability to punish electoral infractions in both last January's election and October's referendum. The commission conceded that instances of fraud had occurred, but its critics say it did little to rectify them or punish the perpetrators. Nor did the commission do much during the campaign before the December polling, when anti-UIA campaign workers were attacked and several reportedly killed. The Shia parties have also apparently used their control of the interior ministry to murder Sunni leaders and of the de-Baathification committee to end Sunni political careers by decree.

National disunity

Given that many hoped the 2005 elections would woo Sunni Arabs towards peaceful politics and away from the

insurgency, the current exchange of accusations over the election is a nasty setback. The only way out of the mess, say many Iraqis, is to form a genuinely national government in which the Sunnis are offered ministries, thus showing them that they do indeed have a stake in the system.

President Jalal Talabani, who prides himself on his ability to win support beyond his Kurdish brethren, has brought leaders of all three major ethnic and sectarian groups up to the Kurds' northern self-rule area to talk about a national-unity government. Both Shias and Sunnis have recently made encouraging noises about forming a “balanced” and “non-sectarian” government.

But a national-unity government would bring its own problems. Ministries tend to become fiefs of particular political forces. That is undesirable in any country, but particularly so in Iraq, where the auditing of budgets swollen by petrodollars is minimal and ministerial bodyguards with their uniforms and weapons licences are useful tools for abducting and murdering people. Part of the Shias' reluctance to hand over a powerful ministry to a former Baathist is that he would almost certainly turn it into a centre of power and patronage for his former cronies.

However, creating a smoothly functioning state is too much to hope for in Iraq just at the moment. The priority is to involve in government those Sunnis who have been undermining it. The hope is that giving militia chieftains and former insurgents titles and budgets will also give them a stake in the system. Getting them to govern cleanly and effectively is a problem for the future.

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CLASSIC
PERTH 2006

Congo

A giant leap forward

Jan 5th 2006 | KINSHASA
From The Economist print edition

After a successful vote, more to follow, with luck

CONGO held a referendum on December 18th. In most countries, this might not mean much. But Congo is different: it has not held an independent election in over 40 years. After decades of dictatorship, war and chaos, the referendum was not so much a huge step as a giant leap in the right direction.

Though the results are still trickling in from across the country, it seems that over 80% of Congolese have accepted a draft constitution that sets up new institutions, paving the way, with luck, to a functioning government and bureaucracy. But, more important, the vote was also a relatively successful dry-run for a clutch of delayed local, parliamentary and presidential elections that must be held by the middle of this year.

The UN believes that Congo's elections are the most complicated it has ever been involved in, and it is easy to see why. Congo is vast, two-thirds the size of western Europe, but it has scarcely any decent roads. Material for the referendum had to be air-lifted by helicopters, ferried by dug-out canoes and carried through the jungle on people's heads. The UN also maintains nearly 17,000 soldiers in Congo. They are supposedly trying to control the thousands of militiamen who were used by various factions in the country's civil and other wars, and who continue to roam around the east of the country.

The vote presented problems, of course. Many Congolese had no idea of what they were being polled on. “Yes, I've heard about this vote on Sunday. I think I will go but I'm not sure which person I will vote for,” said Monique, a smoked-monkey seller in the remote jungle town of Mbandaka, a few days before the poll. Others, in South Kivu province, for example, which Rwanda until recently occupied, were not much better informed. An adviser to the president, Joseph Kabila, said, “People in the east were told to vote yes for President Kabila and vote no if they wanted the Rwandans back.”

Heavy-handed government tactics were in evidence elsewhere. Theodore Ngoy, a former ally of Mr Kabila who became one of the no campaign leaders, tried to hold a peaceful rally in Kinshasa days before the vote, but he was arrested and his supporters were dispersed with police bullets. In the end, however, international observers, led by the European Union's, said the referendum was free and fair. Over half the 25m registered voters cast a ballot, mostly for the first time, and the bands of gunmen did not disrupt the polls.

Much remains to be done, however. During the rule of Mobutu Sese Seko, the dictator who died in 1997, Congo—which was then called Zaire—became a byword for corruption, with hundreds of millions of dollars going missing from the state coffers. Analysts say that graft may not be quite as spectacular now, but the problem remains serious.

And the east is still lawless. Days after the referendum, UN and Congolese soldiers attacked militiamen in Ituri in the north-east and Ugandan rebels in North Kivu province. About 80 rebels were killed. This may stop President Yoweri Museveni of Uganda from threatening to invade Congo to hunt down the rebels, at least for a while, but it will not solve any other problems. About 10,000 Rwandan Hutu fighters, for instance, also remain at large in the east. Since at least some of them took part in Rwanda's genocide in 1994, the Rwandan government has used their presence as a pretext to invade Congo in the past.

Disarming the gunmen is urgent. But there is also an entire state to rebuild. The national army is a mess, law and order is non-existent and no ordinary Congolese receives medical care unless he is lucky enough to get it from an international aid agency. Even so, argues Ross Mountain, the deputy head of the UN mission in Congo, the high turnout for the referendum showed “the extent of the desire of the population for change and getting beyond 40 years of misrule”. Similarly successful elections this year would be another giant leap in the right direction.

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CLASSIC
PERTH 2006

Tanzania

Business as usual

Jan 5th 2006 | DAR ES SALAAM
From The Economist print edition

Only one surprise in the Tanzanian elections

AP

Jakaya Kikwete: Tanzania's progressive new president

THE election of Jakaya Kikwete as Tanzania's fourth president, on December 14th, was widely expected. It was the margin of his victory that turned heads. Mr Kikwete took 80% of the vote in the presidential election. The Party of the Revolution, or Chama Cha Mapinduzi (CCM), of which Mr Kikwete is the sleekest apparatchik, did even better, winning 206 of 232 parliamentary seats. That was a bitter blow for a fractured opposition that had hoped to win 100 seats and establish a genuine multi-party democracy in Tanzania for the first time.

Mr Kikwete, one of Africa's longest-serving foreign ministers, played well everywhere except on the slopes of Kilimanjaro and in the semi-autonomous islands of Zanzibar—two regions where government heavy-handedness has reduced the regimented appeal of CCM. The ruling party tampered with the results in both the presidential and the parliamentary election when Zanzibar voted last October, perhaps foiling an opposition win there. Cynical foreign diplomats in Dar es Salaam who held their peace then lest they should annoy CCM and perhaps encourage violence, may feel vindicated. CCM dominates the 35m strong mainland, whereas Zanzibar has but 1m people. Skirmishes in Zanzibar since the mainland voted in December have been limited, so far, and CCM has made extravagant promises about better schools and health care for the islanders, to try to keep them quiet for another five years.

Mr Kikwete says he is proud to represent a “beautiful, peaceful and united nation”. Tanzania is all those things, though the union between Zanzibar and mainland Tanganyika remains perpetually fragile, despite the best efforts of CCM, with its peculiar talk of togetherness, signature green uniforms and credulous local political officials. Moreover, the sense of amity promoted by the party has been accompanied by decades of foggy socialist economics that has left Tanzania one of the poorest countries in Africa, even though it has received large quantities of aid.

With luck, the new president will continue the trend of his predecessor, Benjamin Mkapa, towards free-market reforms that might help to reverse some of the economic follies of the past. GDP is expected to grow by 6% this year and foreign investment to increase, helped by a relatively low crime rate and a growing tourism industry. But questions remain as to whether some privatisations will actually happen and whether the government will be able to keep a larger share of the burgeoning revenues from gold-mining concessions for itself.

The stability implied by the election has given rare comfort to foreign donors who believe development money, correctly applied, can foster good government. That view, based more on faith than example, has taken a battering of late with Uganda veering towards autocracy and Ethiopia possibly reverting to the bloody excesses of its Marxist past. A self-styled “fourth phase” for CCM is hardly cause for celebration, but it does offer some hope of eventually expanding Tanzania's economy in ways that still preserve the country's peaceable nature.

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PERTH 2006

African optimism

The hopeful continent

Jan 5th 2006 | JOHANNESBURG
From The Economist print edition

Africans hang on to their rose-tinted spectacles

THEY may not be the richest, but Africans remain the world's staunchest optimists. An annual survey by Gallup International, a research outfit, shows that, when asked whether this year will be better than last, Africa once again comes out on top. Out of 52,000 people interviewed all over the world, under half believe that things are looking up. But in Africa the proportion is close to 60%—almost twice as much as in Europe.

Africans have some reasons to be cheerful. The continent's economy has been doing fairly well with South Africa, the economic powerhouse, growing steadily over the past few years. Some of Africa's long-running conflicts, such as the war between the north and south in Sudan and the civil war in Congo, have ended. Africa even has its first elected female head of state, in Liberia.

Yet there is no shortage of downers too. Most of Africa remains dirt poor. Crises in places like Côte d'Ivoire, Sierra Leone and Zimbabwe are far from solved. And the democratic credentials of Ethiopia and Uganda, once the darlings of western donors, have taken a bad knock. AIDS killed over 2m Africans in 2005, and will kill more this year.

So is it all just a case of irrational exuberance? Meril James of Gallup argues that there is, in fact, usually very little relation between the survey's optimism rankings and reality. Africans, this year led by Nigerians, are consistently the most upbeat, whether their lot gets better or not. On the other hand, Greece—hardly the worst place on earth—tops the gloom-and-doom chart, followed closely by Portugal and France.

Ms James speculates that religion may have a lot to do with it. Nine out of ten Africans are religious, the highest proportion in the world. But cynics argue that most Africans believe that 2006 will be golden because things have been so bad that it is hard to imagine how they could possibly get worse. This may help explain why places that have suffered recent misfortunes, such as Kosovo and Afghanistan, rank among the top five optimists. Moussaka for thought for those depressed Greeks.

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Italian politics

Prodi's unhappy new year

Jan 5th 2006 | ROME
From The Economist print edition

IBERPRESS

A new scandal threatens to dent the centre-left's election chances

FEW European countries face a more crucial year than Italy. A general election on April 9th will decide whether Silvio Berlusconi's centre-right coalition, elected in 2001, continues in office. The controversies that always surround Mr Berlusconi, and even more his disappointing management of the economy, have made his government deeply unpopular. Italy badly needs radical reform, yet Mr Berlusconi's coalition, notionally committed to economic liberalism, has done precious little in its five years in office.

Thus a much-hyped shake-up of the pension system will not now take effect until 2008. Labour-market reforms have been started but not expanded. A strengthening of the country's corporate-governance laws, pushed through just before the end of 2005, was a delayed response to the Parmalat scandal of 2003. And the economy has stuttered since Mr Berlusconi came to power. Most estimates of GDP growth last year are coming in at no more than 0.2%. This year Italy will once again have the slowest-growing economy in the European Union.

The centre-left opposition, led by a former prime minister (and former president of the European Commission), Romano Prodi, could hardly have wished for a more propitious start to an election year. But its new-year euphoria lasted all of 24 hours. By January 2nd, the formerly communist Left Democrats (DS), the biggest party in Mr Prodi's alliance, the Union, was in crisis. A Berlusconi-backed newspaper, *Il Giornale*, had published extracts from a telephone call recorded by magistrates that puts the party's secretary-general, Piero Fassino (pictured above, talking to Mr Prodi), centre stage in Italy's long-running scandals over bank takeovers. These have already led to the arrest of several bankers and to the downfall of the Bank of Italy's governor, Antonio Fazio.

Mr Fazio fell amid claims that he had blocked the purchase of Banca Antonveneta, by a foreign lender, ABN AMRO, backing instead a bid by an undercapitalised rival, Banca Popolare Italiana (BPI). Meanwhile another Italian financial concern, the insurance firm Unipol, was battling another foreign bank, Spain's BBVA, for control of Banca Nazionale del Lavoro (BNL). It is around this second bid that the latest controversy has erupted.

Although it is publicly quoted, Unipol is controlled by Italy's co-operative movement. Since 1999, its has pursued an aggressive policy of acquisition, more than quintupling its premium income. The telephone transcripts, whose authenticity has not been questioned, make clear that Mr Fassino sees this eminently capitalist predator as an extension of his party. After being given details of Unipol's bid for BNL by the company's chairman, Giovanni

Consorte, Mr Fassino is quoted as exclaiming: “So then. We're the bosses of a bank.” He then hastily corrects himself, saying, “You are the bosses of the bank. I have nothing to do with it.”

Mr Fassino's spokesman has stressed that the transcripts offer no evidence of wrongdoing: the party leader was merely gathering information. The publication of his remarks by a newspaper belonging to the Berlusconi family is surely part of a campaign to discredit the centre-left.

No doubt this is true. But it is also beside the point. Unipol, with its headquarters in “red” Bologna, on Via Stalingrado, was supposedly a model of all that the left can bring to capitalism. The home page of its website is plastered with such words as “transparency” and “ethics”. Yet, with the apparently wholehearted support of the DS's leader, it has embarked on an audacious bid that is claimed to have involved several irregularities.

Unipol outbid BBVA by recruiting the support of a group of property developers, some of whom were also involved in the BPI fight with ABN AMRO. Prosecutors believe that central participants in both bid battles secretly helped each other to build up their shareholdings. They also claim that Mr Consorte and his chief executive obtained unsecured loans of €4m ($4.8m) from BPI that were used for trades that netted each €1.7m.

Unipol is under investigation for its role in both bids. Mr Consorte resigned as chairman last month after being questioned by investigators. He is also under investigation in Milan for alleged market-rigging in connection with the bid for Banca Antonveneta, and in Rome for the same activity in relation to the offer for BNL.

Italy's stockmarket regulator had already ordered Unipol to raise its bid after discovering that the insurer had increased its holding in BNL through an undisclosed agreement with Germany's Deutsche Bank. BNL has complained about the structure of Unipol's offer, both to the courts and to regulators. Small wonder that the bid is still awaiting formal approval six months later—a potential early headache for Mr Fazio's successor, Mario Draghi (see article). Small wonder, too, that some on the left are so dismayed by protests from the DS leadership that nothing is amiss.

“I talk to a lot of people from the grassroots of the DS,” commented the Nobel laureate, Dario Fo. “They are furious about Unipol. They feel betrayed and above all indignant over the shadow that has been cast over the history of the co-operative movement.” A veteran DS leader and former minister, Giorgio Napolitano, has said that Mr Fassino should at least admit that he has misjudged both Mr Consorte and the implications of Unipol's strategy. Peppino Caldarola, a former editor of the party daily, *L'Unita*, says he is “embittered, bewildered and disappointed”.

Foreign investors could be forgiven for sharing at least some of these sentiments. Quite apart from the potential damage it may do to the centre-left's election hopes, Mr Fassino's involvement with Unipol threatens further to dent Italy's reputation in the international business world, already battered by the Parmalat and Fazio affairs. It reinforces a view of Italy as a country in which entrepreneurs need political patronage to succeed. Just as important, it suggests that political leaders, of left and right alike, remain incorrigibly protectionist at heart.

In this, of course, they are faithfully mirroring general social attitudes. Among the myriad words penned and broadcast on the Unipol affair barely any have condemned a venture that was so manifestly at odds with Italy's commitment to liberalise and to opening its markets to EU and other foreign investors. Italy's atavistic protectionism and disdain for freer markets both play a large part in holding back its economy—and will not necessarily change even if its government does.

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The Bank of Italy

Super Mario flies in

Jan 5th 2006 | ROME
From The Economist print edition

A new governor may, with luck, mean a new start for a troubled institution

Reuters

Draghi's ring of confidence

A SHORT Christmas break was all that the Italian government needed to pick Mario Draghi as governor of the Bank of Italy. He will take over from Antonio Fazio, who resigned on December 19th. Mr Fazio's departure brought to an inglorious end a scandal that erupted last summer, after telephone intercepts were published suggesting that he had leant unusually far in favour of a bid by Banca Popolare Italiana, a shaky domestic bank, for Banca Antonveneta, rather than a rival bid by a Dutch bank, ABN AMRO (which eventually won the day despite Mr Fazio's efforts).

Mr Draghi has spent four years as a vice-chairman at Goldman Sachs, based in London. Such top-level experience in international finance augurs well for his new job. His predecessor's downfall owed much to a parochial view of how best to manage the bank. Mr Draghi will breathe fresh air into the musty corridors that Mr Fazio walked.

One dossier that Mr Fazio left open is another controversial takeover, of Banca Nazionale del Lavoro (BNL) by Unipol, an insurer. This bid too is under investigation by magistrates, and is now having political ramifications (see article). If the central bank's general manager, who fills in until Mr Draghi arrives on January 17th, manages to approve the deal, Mr Draghi may be relieved: Goldman Sachs advised BBVA, a Spanish bank, in its rival bid for BNL last year.

Besides shaking up Italy's banks, the most pressing task for the new governor will be to restore morale. Once the country's most respected institution, the Bank of Italy's standing was battered by last year's banking scandals. Fortunately, Mr Draghi has a record of boosting spirits. He was director-general of Italy's Treasury for over ten years. When he arrived in 1991, he found a bureaucratic backwater with demotivated staff who would rather be working at the Bank of Italy. But his staff soon cheered up.

Why? Partly, because political changes in the 1990s made the work of the Treasury more interesting. It was involved in new legislation for the financial-services industry; it led Italy's drive towards privatisation; and the pressing need to make the Italian economy fit to join the euro brought it new power. Mr Draghi hired bright, ambitious people, some of them from the Bank of Italy itself. Under his aegis, the Treasury even took control of some matters that the bank had previously handled, such as management of public debt and European Union policy.

As the Treasury's star has waxed, so the Bank of Italy's has waned. The euro's arrival may have deprived the central bank of its monetary-policy autonomy, but it now has a much greater responsibility for liberalising and opening up to competition Italy's banking sector. Mr Fazio encouraged some domestic bank mergers, but ducked the rest of that agenda. It will now be up to Mr Draghi to take it forward instead.

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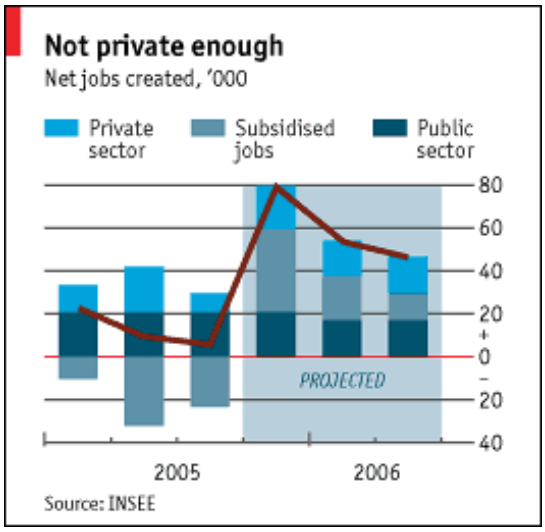
Unemployment in France

Down, down

Jan 5th 2006 | PARIS
From The Economist print edition

More jobs, but few in the private sector

AMID the prevailing gloom in France, some cheerful news has begun to trickle out. Unemployment fell for the sixth month in a row in November. At 9.6%, it is still woefully high, and well above the euro-zone average of 8.3% (unemployment also fell sharply in Germany in November). But economists reckon it could drop below the significant level of 9% by the end of 2006—a level not reached since 2002.



What explains this fall? Only a small part is due to economic growth. The economy expanded by just 1.5% in the first three quarters of 2005, and may do little better in 2006. This has yielded some new jobs: in 2005, nearly 60,000 more jobs were created than lost in the non-farm private sector, after a flat year in 2004. A new two-year job contract has also helped. Introduced by Dominique de Villepin, the centre-right prime minister, it gives employers of fewer than 20 workers more flexibility. These firms use this contract for roughly one in ten of the new jobs they create.

A second explanation is demographic. France has one of Europe's highest birth rates, but its population is nonetheless ageing. With baby-boomers beginning to retire, and fewer leaving school, the number seeking work is now dwindling. Some 29,000 more newcomers will come to the labour market than retire this year, around a quarter as many as in 2004.

The biggest reason for the falling jobless figures, however, is social policy. As the chart shows, the number of new subsidised jobs set up under the government's “social cohesion” plan began to swell in late 2005. In the first half of this year, INSEE, the official statistics body, forecasts that, out of a total of 100,000 new jobs, one-third will be in the private sector, another third in the bureaucracy and the remaining third will be state-subsidised. This last category of jobs varies from positions in voluntary organisations and town halls to schools and sports clubs.

At the same time, the government has clamped down on unemployment benefit. All long-term unemployed young people have been called in for interviews, to be placed on job or training schemes. Anybody who is long-term out of work and accepts a job gets a €1,000 bonus. All benefit claimants are now required to sign on more regularly than before. These measures have helped to improve the unemployment figures.

If the fall in joblessness is partly engineered, it remains, at least in the short run, politically astute. Job insecurity and worries about competition from lower-wage countries have been a main cause of France's sagging morale, and its rejection of the European Union's constitution last year. Indeed, although Mr de Villepin will claim credit for better job figures in the months ahead, many of the measures were actually put in place before he took office, by Jean-Louis Borloo, the “social cohesion” minister.

The need to deal with joblessness became more acute after the recent riots in the suburbs. This week, the government lifted the state of emergency, imposed to curb the violence, after only 425 vehicles were burned on New Year's Eve—a number considered relatively normal. Getting residents of public housing projects into work is more urgent than ever.

The great missing element, however, remains private-sector job-creation. The obstacles are well documented: complicated rules for laying off workers, high social charges for employers, strict working-time rules and a high minimum wage. The new two-year job contract helps a bit, though only for small firms. Some other ideas are on

the table. President Jacques Chirac is talking of shifting the financing of the benefit system away from the payroll tax. “Because it weighs too exclusively on wages,” he said this week, “the system of financing social protection works against jobs.”

The solution is less clear. Mr Chirac mentioned a value-added employers' charge. Others have talked of a social VAT. Yet Mr Chirac's past new-year promises have often turned out to be empty. As he approaches his 11th anniversary this spring, and with a presidential election due in 2007, nobody any longer holds out hope of serious labour-market reform.

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Albania's electricity shortages

Lights out

Jan 5th 2006
From The Economist print edition

A more humdrum energy crisis than Ukraine's

AFP

A candle in the wind

THE focus of world energy buffs may have been on Ukraine this week. But parts of the western Balkans have their own energy crisis. Keeping the lights on in Tirana this winter has proved too hard for KESH, Albania's state-owned electricity utility. Low rainfall and a failure to maintain ageing hydropower plants that produce 90% of the country's electricity meant that, for much of November and December, the capital was subject to daily power cuts lasting as long as 18 hours.

Sali Berisha, the centre-right prime minister, says that boosting the power supply is his overriding priority. Mr Berisha's Democratic Party won power last July by pledging reforms, including an end to electricity shortages. Mr Berisha has scrapped two big transport projects for Tirana launched by his Socialist predecessor—a high-speed train link with the airport and a multi-level highway junction—as unnecessary while power cuts are so common.

One problem is that KESH is so short of cash. Subsidies are being cut. The utility has tried to raise revenues by installing more meters. But electricity theft is rife in Tirana's illegally built suburbs, which provide homes to thousands of poor immigrants from the north.

Under communism Albania sold hydropower to its Balkan neighbours. But domestic demand soared in the 1990s, when Albanians who went to work in Greece and Italy sent money back to their families to buy such whizzy new products as dishwashers, hair-dryers and microwave ovens. The price of electricity imported from Bulgaria and Romania rose when these countries, under pressure from Brussels, liberalised their electricity markets. Albania's parliament has now passed legislation to give the utility greater freedom to buy power from abroad, if it can find it. Genc Ruli, the energy minister, struck a deal with distributors in Bulgaria and Romania just in time to prevent big black-outs in Tirana over new year.

With other countries in the region, Albania signed a European Commission-sponsored energy treaty in Athens last October. The pact is meant to promote co-operation by setting up a regional energy market. Yet one diplomat calls the treaty “admirably high-minded, but impracticable at present”. It would cost more than $15 billion to build the infrastructure necessary for a proper electricity market across the region, says the World Bank. Albania, the second-poorest country in Europe after Moldova, would struggle to pay.

KESH now plans Albania's first thermal-power plant, a small 120-megawatt unit, near the port of Vlora. Local residents and green groups say it makes no sense to build a power station next to a town that is meant to be a

magnet for future tourists. But without reliable power, foreign tour operators, like other foreign investors, will continue to give Albania a miss.

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Denmark and Islam

Prophetic insults

Jan 5th 2006 | COPENHAGEN
From The Economist print edition

Free speech clashes with religious sensitivity

FOR much of last year, various squabbles have simmered over several prominent Danes' rude comments about Islam. Now a schoolboy prank by a newspaper has landed the prime minister, Anders Fogh Rasmussen, in the biggest diplomatic dispute of his tenure in office.

The latest spat started some months ago when *Jyllands-Posten*, Denmark's biggest-selling broadsheet, published a dozen cartoons depicting Muhammad. Visual representations of the prophet are frowned upon by the faithful. And *Jyllands-Posten*'s cartoons were undeniably strong stuff: one showed Muhammad in a bomb-shaped turban, another depicted him wielding a cutlass and a third had him saying that paradise was running short of virgins for suicide-bombers. The paper insists that it meant no offence: it was merely protesting against the self-censorship of some cartoonists who had refused to illustrate a children's book about Muhammad for fear of reprisals. But the result has been a row that has spread far beyond Denmark's borders.

Louise Arbour, the United Nations human-rights commissioner, said she was “alarmed” by such an “unacceptable disregard for the beliefs of others”. Similar condemnations came from the European Commission, the Council of Europe and the Arab League. The affair has led to protest marches in Copenhagen and Karachi, and a wave of disapproving e-mails to Danish embassies. The cartoons were even condemned by many in Denmark's liberal-minded intelligentsia, not because they favour censorship but because they see the drawings as part of an increasingly xenophobic tone that has infected all Danish dealings with foreigners.

In a country where a member of parliament can liken Muslims to “cancer tumours” and still not lose her seat, unfettered public debate is seen as normal. Danes, like most people, cherish their freedom of speech. But their secular society may have blinded them to some people's religious sensitivities. Uffe Ellemann-Jensen, a former foreign minister, laments his country's lack of manners. “We have a right to speak our minds, not an obligation to do so,” he says.

Mr Fogh Rasmussen has tried to defuse the row mostly by ignoring it. After he had rejected a request for a meeting with 11 ambassadors from Islamic countries to Copenhagen, he was lashed by 22 former Danish ambassadors to the Muslim world, who deplored his ignorance of diplomatic niceties. After several more weeks of dithering, the prime minister at last tackled the matter in his new year's speech, condemning any attempts “to demonise groups of people on the basis of their religion or ethnic background”. But although he alluded to “a few unacceptably offensive” instances, he did not mention *Jyllands-Posten* by name. And he also insisted that the general tone of the Danish debate was “civilised and fair”.

For many Muslims, this is too little, too late. Ahmed Said Kassem, a leading Copenhagen Muslim, has called on *Jyllands-Posten* to apologise and on the government to dissociate itself from the cartoons. In a sign that the row may have some time still to run, the Organisation of the Islamic Conference, a 57-strong group of countries, has also announced a boycott of “Images of the Middle East”, an exhibition due to be held in Denmark this summer. What should have been a celebration of Denmark's cultural links with the Islamic world now looks like falling victim to Danish free speech.

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CLASSIC
PERTH 2006

Hungarian politics

Wrap up

Jan 5th 2006 | BUDAPEST
From The Economist print edition

A squabble about a newspaper, a fur coat and an election

Gyurcsany on show

AS ONE of the country's richest men, Ferenc Gyurcsany can afford the sleekest of fur coats. So it was something of a surprise to find the Socialist prime minister appearing in an advertisement wrapped in a scraggy-looking pelt. But then one realised that the advertisement had been placed by the main opposition party, the right-wing (and increasingly populist) Fidesz.

The ad's trigger was, rather improbably, a survey of Hungary published in the *Financial Times* last month. One line of the survey provoked much gnashing of teeth at Fidesz's headquarters: "In spite of dangerous imbalances in the economy, Hungarians are better off than ever on average." When the Socialists quoted selectively from this report to their advantage, Fidesz placed advertisements claiming that the government had paid the *Financial Times* a *Bunda* (a fur coat, but also slang for a bribe) of 20m forints ($95,000) to secure favourable editorial copy.

The government had indeed paid such a sum, but for advertisements in the survey that were clearly marked as such. With an election likely to take place in April, and the Socialists narrowing Fidesz's lead in the polls, Fidesz leaders seem to think that they must snatch any opportunity to knock the government. It speaks volumes for the insular nature of Hungarian politics that nobody seemed to grasp that their advertisement might also be libelling the *Financial Times* and its journalists, who have reacted angrily and demanded an apology and a retraction.

Bashing the foreign press is a popular pastime for Fidesz supporters during elections. In the 2002 campaign a mysterious cabal known as the Kontroll Csoport (Control Group) drew up a list of foreign correspondents supposedly guilty of the thought-crime of "anti-Hungarianness", and published it in the pro-Fidesz *Magyar Nemzet* newspaper. Things turned nastier when several right-wing journalists then appeared on television and verbally abused people on the list, using both anti-Semitic and homophobic slurs.

Fidesz, which was then in power, denied any connection to the Kontroll Csoport. Yet curiously, after a western diplomat had told a government spokesman that such behaviour was not encouraged in countries that wished to join the European Union, it stopped immediately. And *Magyar Nemzet* performed a prompt U-turn, publishing a series of laudatory articles about those on the Kontroll Csoport list.

This time around Fidesz has taken a more conciliatory position from the outset. When the Hungarian International Press Association issued a statement condemning the *Bunda* advertisements as a slur on the integrity of both the *Financial Times* and its correspondents, Fidesz claimed that the whole thing was a misunderstanding and praised the country's "much-valued" foreign press corps. But the *Financial Times* is still waiting for an apology.

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Charlemagne

Back from the dead

Jan 5th 2006
From The Economist print edition

What part of "no" do European integrationists not understand? Every part, apparently

IN ONE ancient fable, a frog falls into a pail of milk. Unable to scramble out, the creature thrashes around, seemingly drowning. Eventually, however, his frantic struggles churn the milk into butter—and he hops away. Some European Union leaders seem to see themselves as this frog. They suffered a huge defeat over the EU constitution, but they think that, if at first they did not succeed, they should just try, try again.

That, at any rate, may explain attempts to resurrect a constitution that only six months ago seemed to have been killed by French and Dutch voters. Germany's chancellor, Angela Merkel, told the *Frankfurter Allgemeine Zeitung* that "this constitution has so many positive elements that we must not abandon it." Both her spokesman and the leader of her party in the European Parliament say that reviving the constitution will be Germany's top priority when it takes the EU's rotating presidency in the first half of 2007. If it fails, says Portugal's president, José Socrates, Portugal will take up the task in the second half.

Perhaps integrationists will get their wish even sooner. Wolfgang Schüssel, Austria's chancellor, is in charge of the EU just now, and he insists that the constitution is not dead. In theory, the EU is in the midst of a year-long "pause for reflection", which its leaders decreed after the French and Dutch referendums. But why wait? The Austrians are talking of working out by the middle of 2006 how to take the constitution forward. Yet this drift towards reviving a dead text has as much plausibility as the Danube suddenly turning blue. All 25 EU members must ratify the constitution before it can come into force—and that seems an impossibly remote prospect.

It might have been possible to wiggle out of the unanimity requirement, or to insist on a second referendum, if the refusenik were a single small country, or an awkward cuss, such as Britain. But France and the Netherlands, both founder members, cannot be either sidelined or wished away. Their present leaders could not possibly risk the voters' wrath by trying to pass in parliament a charter that had been rejected by the people. No serious politician in either country has been foolhardy enough to call for a new referendum.

Besides, the French and Dutch are not isolated. Britain would be likely to reject the constitution if it were put to the vote. So might Sweden or Denmark, and perhaps one or more of the central Europeans. Thus, quite apart from the little question of respecting the will of the people when they have spoken, demands to resurrect the constitution run up against the practical problem that half a dozen countries cannot now ratify it.

Why are people falling over themselves to promote something that cannot succeed? Perhaps the politicians think they can change voters' minds. They did so after 1992, when Denmark rejected the Maastricht treaty, and again after 2001, when Ireland rejected the Nice one. The politicians may even be right this time, too: the voters may change their minds—one day. But at present support for the EU is falling, suggesting that the constitution may be even less popular than it was.

Perhaps some of the politicians calling for a revival of the constitution are simply trying to burnish their European credentials. Ms Merkel might be calculating that a bit of windy Euro-talk is an easy way to establish herself as the true and only heir to the Europhile Helmut Kohl. Or perhaps, to be more generous, European leaders genuinely believe that the EU is unworkable without the institutional reforms in the constitution, such as the new voting rules, a separate foreign minister and the abolition of the musical-chairs presidency. In this, too, they may be right. But even if they are, the politicians are going a funny way about getting matters changed, since sticking with the whole constitution and nothing but the constitution will make it even harder to rescue any of its useful bits. It would surely be easier to try to carve up the corpse for the organs, rather than to try to jolt the whole thing lumberingly back to life.

The fact is that this is one of those moments when the EU's integrationist impulse is overriding both democracy and natural caution. The budget crisis is over and there is no other displacement activity (except perhaps energy security). The pretence of a pause for reflection has been largely abandoned. The text of the constitution also encourages ratification to continue despite the French and Dutch rejections. Fourteen countries have now ratified it, setting up the possibility, envisaged in a declaration annexed to the treaty, of a showdown with the few that have not.

The perpetual-motion machine

Indeed, Europe's integrationist drive is so strong that it keeps popping out. Guy Verhofstadt, prime minister of Belgium, has written a book, “The United States of Europe”, that argues for closer co-operation (including political co-operation) among the 12 euro-zone countries. Such demands for integration are so strong that something is likely to come of them, though whether it is co-operation within the euro zone, sovereignty-sharing arrangements under the existing treaties, or cherry-picked bits of the constitution is hard to say.

But to go back to the constitution as if nothing had happened—or to argue that what happened was so long ago that nobody should worry about it—seems a dangerous strategy. It risks precipitating a huge split between the countries that want the constitution and those that do not, as well as alienating long-suffering voters everywhere.

Before they go down this road, Europe's leaders might ponder another fable, this one by Aesop. The frogs are living happily in a pond, until they decide they need a proper king (and constitution). They ask Jove for one. First he sends a log, but they get bored by such a passive ruler. Then he sends an eel, but it proves too easygoing. So the frogs demand another ruler, and an infuriated Jove sends them a heron—who eats them all.

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Race relations

Multiculturalism and its discontents

Jan 5th 2006 | BIRMINGHAM AND LEICESTER
From The Economist print edition

The changing face of racial conflict in Britain

Get article background

IN 1985, the MP Enoch Powell issued a prognostication of doom. By the end of the 20th century, he claimed, fully 8% of Britain's population would be black or brown-skinned, and a third of the residents of some cities would be non-white. The result, he thought, would be a nation “unimaginably wracked by dissension and violent disorder”.

Few took Powell's forecast seriously. He had been a familiar anti-immigrant bugbear since 1968, when he was exiled from the Conservative front bench for fulminating against “wide-grinning piccaninnies” and seeming to anticipate race war between blacks and whites. Powell's later prediction was almost spot on, though. At the time of the 2001 census, the ethnic minority population of Britain was, indeed, 8.1%. White Britons made up less than two-thirds of the populations of Leicester and Birmingham (and accounted for barely half of all children in those cities). Powell was also right to forecast some inter-racial strife, but he was wrong about which groups would be fighting.

These days, members of ethnic minority groups rarely clash with whites or white-dominated institutions such as the police. In the past 20 years, Britain's police have squared off against a violent black crowd only once. Attacks by white mobs on immigrants, of the sort that blighted Sydney's beachfront neighbourhoods last month, have been virtually unknown since the 1950s. But tensions between people of a similar hue have increased. The reasons have to do with the changing geography of the inner city, and, ironically, with the policies that were put in place to avoid the sort of strife that Powell forecast.

In October, violence between Afro-Caribbeans and South Asians erupted in a Birmingham neighbourhood that, 20 years ago, hosted old-fashioned riots against the police. Trouble began when a pirate radio station and the black press aired rumours that a black girl had been raped by a gang of Pakistani men in Lozells Road. Boycotts against Asian businesses were followed by stone-throwing, street fights, the desecration of Muslim graves and the murder of a black man.

Leicester, a generally more placid city, is also blighted by tensions between South Asians and Afro-Caribbeans. But there, fissures are as much between cultural groups as racial groups. “Most of the aggravation flies between the faiths,” according to Manzoor Moghal, a prominent South Asian Muslim. There is resentment at Muslims' growing political assertiveness, which derives partly from sheer numbers (Muslims were 4% of Leicester's population in the early 1980s, and 11% in 2001) and partly from the fact that their votes are concentrated in a few wards. Another rubbing point, which has sparked violence in schools, is between British-born Afro-Caribbeans and newly arrived Somalis.

When Mr Moghal came to Leicester (with many others) as a refugee from Idi Amin's Uganda in the early 1970s, crude white racism was the rule. Together with blacks, South Asians were condemned by the National Front, a far-right political party. They were discriminated against by white employers, landlords, the police and the council, which had taken out an advertisement in a Ugandan newspaper warning them to avoid the city. As he puts it, “I had escaped one form of racism only to find another.”

Whatever happened to white racism? It probably did not decline as a result of enlightened attitudes, although opinion polls suggest that hostility to Afro-Caribbeans, at least, has dissipated. A more likely explanation is that the most hostile whites have simply abandoned the inner city, taking their votes with them. Around 15,000 whites left Leicester during the 1990s. Some of those who remain live on estates that are separated from black and Asian neighbourhoods by the city centre and a busy road.

Whites are nonetheless numerous enough to spur conflict, even if they do not instigate it. Alex Kamanga, who runs the Afro-Caribbean centre in Leicester, says that black Caribbean children resent Somali immigrants in part because they upset the black-white modus vivendi in the school playgrounds. In Birmingham, Dal Singh Dhesy, who runs a Sikh community group, complains that the “British” often mistake his co-religionists for Muslims. Since the atrocities of September 2001 and last year's bombings in London, a tense relationship has hardened.

The complex pattern of resentment that prevails nowadays is in one sense less potent than the simple discrimination of the 1970s. Ethnic minority groups no longer have to contend with the combined hostility of the police, the council, and public opinion. But current prejudices are also trickier to tackle now that the downtrodden are often the oppressors. Mr Dhesy complains that public authorities continue to follow assumptions about race relations that are out of date. “If a white man attacks an Asian, it's a racial assault. If a black man attacks an Asian, it's robbery.”

An important reason why racial conflict now tends to involve people with brown and black skin has to do with reforms made by civic authorities and the police in the 1970s and 1980s. Policies that were enacted to avoid racial conflict between blacks and whites mostly proved successful. But they inadvertently laid the groundwork for hostility between non-whites.

Kirk Dawes, a black former police officer who now runs a mediation service in Birmingham, commends the way in which the police and the council have purged overt racists from their ranks. But he criticises the way both have relied on “community leaders,” especially those of a fiery type, as interlocutors with ethnic minority groups. “There is a belief that those who shout the loudest can best solve the problems within their community,” Mr Dawes says. Some of those community leaders were prominent in the protests against Asian shopkeepers in October, which later turned violent.

Birmingham's Asians are more pointed in their criticism. The police, they say, were so keen to avoid offending black sensibilities that they allowed the protests to run out of control. They also failed to shut down a pirate radio station that purveyed hostility against Asians. In that, the police may have been following lessons learned in the past. An attempt to silence a similar station in the 1980s had sparked rioting.

One well-meaning gesture proved particularly damaging. Following the 1985 Handsworth riot, additional support was given to ethnic minority (and particularly black) businesses in the area. This entrenched the view that a certain proportion of shops ought to be owned by people of a particular colour. Fazal Kapasi, a local shopkeeper, says that last year's riots were fuelled by the belief that Asians were taking more than their fair share of business.

But Mr Kapasi, who sells air fresheners emblazoned with the flags of Jamaica, Pakistan, Kurdistan and England, believes that the recent riots were more of a cry for help from the council than an outburst of simmering racial prejudice. Like many others in the area, he is still inclined to believe the best of his neighbours. “I stand behind the counter for eight hours a day, and most of my customers are black. If there was more racism, I would know about it.”

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Holidays

A new package

Jan 5th 2006
From The Economist print edition

Traditional tour firms grapple with the internet

MENORCA or Majorca? It is that time of the year again. The brochures are piling up in travel agents while newspapers and magazines bulge with advice about where to go. But the traditional packaged holiday, a British innovation that provided many timid natives with their first experience of warm sand, is not what it was. Indeed, the industry is anxiously awaiting a High Court ruling to find out exactly what it now is.

Two things have changed the way Britons research and book their holidays: low-cost airlines and the internet. Instead of buying a ready-made package consisting of a flight, hotel, car hire and assorted entertainment from a tour operator's brochure, it is now easy to put together a trip using an online travel agent like Expedia or Travelocity, which last July bought Lastminute.com for £577m ($1 billion), or from the proliferating websites of airlines, hotels and car-rental firms.

This has led some to sound the death knell for high-street travel agents and tour operators. There have been upheavals and closures, but the traditional firms are starting to fight back, in part by moving more of their business online. First Choice Holidays, for instance, saw its pre-tax profit rise by 16% to £114m ($196m) in the year to the end of October. Although the overall number of holidays booked has fallen, the company is concentrating on more valuable long-haul and adventure trips. First Choice now sells more than half its trips directly, either via the internet, over the telephone or from its own travel shops. It wants that to reach 75% within a few years.

Other tour operators are showing similar hustle. MyTravel managed to cut its loss by almost half in 2005. Thomas Cook and Thomson Holidays, now both German owned, are also bullish about the coming holiday season. High-street travel agents are having a tougher time, though, not least because many leading tour operations have cut the commissions they pay.

Some high-street travel agents are also learning to live with the internet, helping people book complicated trips that they have researched online, providing advice and tacking on other services. This is seen as a growth area. But if an agent puts together separate flights and hotel accommodation, is that a package, too?

The Civil Aviation Authority (CAA) says it is and the agent should hold an Air Travel Organisers' Licence, which provides financial guarantees to repatriate people and provide refunds. The scheme dates from the early 1970s, when some large British travel firms went bust, stranding customers on the Costas. Although such failures are less common these days, the CAA had to help out some 30,000 people last year. The Association of British Travel Agents went to the High Court in November to argue such bookings are not traditional packages and so do not require agents to acquire the costly licences. While the court decides, millions of Britons will happily click away buying online holidays, unaware of the difference.

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Congestion charging

Jambusters

Jan 5th 2006
From The Economist print edition

New technology could improve London's congestion charge

DESPITE the doubts, and despite complaints from shop owners, London's congestion charge—introduced in February 2003—has managed to ease the gridlock in the city centre. Traffic is down by 18%, jams by 30%. The scheme's biggest weakness is that it is crude: drivers pay £8 ($14) to enter the zone between 7am and 6.30pm, regardless of how congested the roads are, or how long they stay.

So road-pricing fans are watching trials by Transport for London (TfL) of a new detection system, called tag-and-beacon, with interest. Under such a scheme (used in Singapore and on some European roads) cars are fitted with electronic tags that are read by roadside masts. If the trial is successful, TfL says that the city could switch to the system once the contract to run the congestion charge is re-let in 2009.

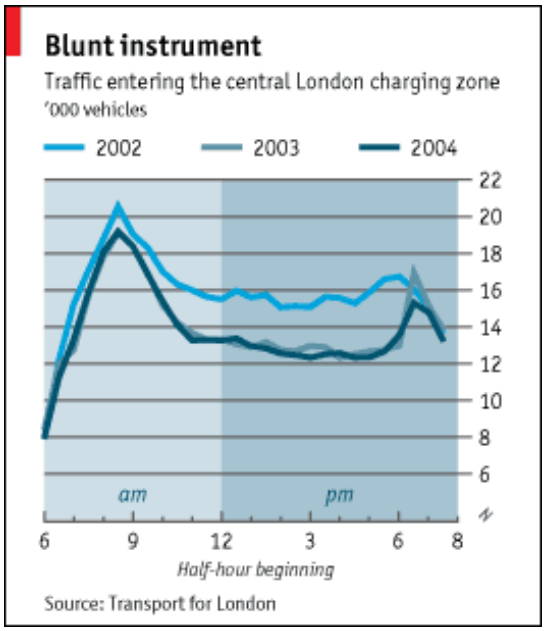
Currently, cameras are used to read licence plates and track motorists. They are not always reliable: an individual camera identifies only around 70% of cars. Most drivers get photographed more than once, which boosts the system's effectiveness to over 95%, but that still leaves several thousand vehicles per day whose details must be laboriously checked by hand. Tag-and-beacon technology is much more accurate, with an identification rate of over 99%.

TfL says the trial is partly designed to see whether the new system could allow drivers to pay charges by direct debit. That would be popular with motorists, who complain that the current payment system is unfriendly: the toll for a day's travel must be paid manually—online, by phone or in a shop—by midnight, with steep fines levied on forgetful drivers.

More precise detection also allows for more precision in policy, and road-pricing enthusiasts see radical possibilities ahead. TfL says it is considering using the new technology to charge drivers each time they cross the zone boundary (up to a daily maximum), instead of paying once for an entire day's travel. That would be cheaper for drivers who make few trips into the zone, although drivers who spend a long time trundling around without leaving (thereby causing the most congestion) would get off lightly, too.

Further refinements may be possible. The current system has cut traffic most drastically in the middle of the day, when congestion is at its lowest (see chart). Demand for road space would better match supply if charges were variable—high at the busiest times of day and low in quiet periods. That would be difficult to do with the current system, which allows many motorists to pass its cameras undetected, but easier with tag-and-beacon.

Such a time-sensitive, variable-charging scheme using a tag-and-beacon system was endorsed last year by Bob Kiley, then TfL's boss, who also said that he wanted to extend the congestion charge to other parts of London. That would be controversial, and Mr Kiley's underlings were quick to insist that his musings were not official policy. But the original scheme was controversial too, yet Ken Livingstone, London's mayor and its biggest backer, was re-elected after introducing it. It would be a shame if timidity took hold now.



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Tony Blair's video diary

Uncandid camera

Jan 5th 2006
From The Economist print edition

A four-minute guide to being prime minister

Get article background

A PRIME MINISTER who has won three elections in a row, who is blessed with an affable manner and a remarkable ability to spin off platitudes like “what is worthwhile is getting things done” without a trace of weariness, has no need of gimmicks to persuade voters that he's just a regular guy doing a very tough job. Or so you might think.

This week “A Day in the Life”, a short video, appeared on the Downing Street website. Everything about the film—the Beatles-inspired title, the shots of the prime minister kicking a football around with some children in between meeting world leaders—reinforces Mr Blair's brand. But it also contains coded messages that only the initiated, or the slightly paranoid, will hear.

First, Mr Blair suggests in the video that being prime minister is terribly hard work. It's a “completely different order of stress, challenge, pressure”. Gordon Brown, Mr Blair's likely successor, and David Cameron, the new Conservative leader, please take note. Mr Brown may have run the economy and amused himself by dabbling in social policy, but late-night stints in the Treasury are nothing compared with the sight of Greenpeace demonstrators dangling from the rafters while you're trying to make a speech. Mr Cameron may be youthful and energetic, but he is untested. Just being leader of the opposition is a big step up, says Mr Blair helpfully. Mr Blair's shoes, it seems, will be hard to fill.

Second, don't badmouth a winner. In the film, Mr Blair cites some wise advice given to him by Margaret Thatcher. Mr Cameron, by contrast, says his party needs to move beyond Thatcherism, and Mr Brown has never been heard praising the woman who also won three successive elections. Of course this principle also applies to Mr Blair: a smart strategist would offer him grudging praise. Mr Cameron, who has done so, may be just ahead of Mr Brown here.

Third, manufacture a cuddly private life. Videos on the White House website show George Bush telling his Scottish terriers about the spirit of the holiday season. Even Vladimir Putin posed with a poodle in his lap in a clip for Russia's “school-age citizens”. Mr Blair and Mr Cameron are both skilled at letting selected details of their domestic lives slip. But Mr Brown could improve. A video of the chancellor reading to his young son or participating in potty training would help, although perhaps not if he is clad in his trademark dark suit and tie.

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University admissions

Learning to live with Offtoff

Jan 5th 2006
From The Economist print edition

Universities are tweaking their intake in the name of fairness

ALONG with the cards depicting jolly Santas and festive reindeer, the Christmas postman brought some young people tidings of great joy—offers of places at university. Prospective doctors, dentists and vets, as well as Oxbridge applicants, will have discovered their fate by now, as will many students who applied for other universities and courses well ahead of the January 15th deadline.

This year's freshers will be starting their higher education in eventful times. In return for being allowed to charge up to £3,000 a year, English universities must now persuade the Office for Fair Access (OFFA, inevitably known as Offtoff) that they are straining to admit students from social classes, ethnic groups, families and schools that haven't traditionally sent many young people to university.

Although there are new grants and bursaries for the poorest students, and fees don't have to be repaid until after graduation, many have fretted that debt aversion might reverse the modest upward trend in working-class student numbers. But these fears seem to have been overblown. Leaked figures appear to show that applications are down by around 5% on the same time last year. But last year was an aberration. Applications were up 8% on the year before, presumably because of students rushing to beat the fee increase.

When the access watchdog was first proposed, it was widely derided as a sop to Labour backbenchers unhappy about the principle of variable fees. But it seems to be potent enough to be having some effect on universities' admissions procedures. A recent report from Universities UK, a body representing university vice-chancellors, describes the tortuous efforts of more than 30 institutions to “widen participation”. Some of the schemes are general (open days; school visits by undergraduates). Some are targeted (Loughborough's “Women into Engineering” and Liverpool Hope's “Black Science” summer schools). And some are remarkably specific (Bristol's three-week law course for teenage mothers; Hull's mentoring scheme for young people in public care).

Others, though, are directly interventionist. Birmingham and Newcastle universities allow students at some poorly performing state schools to fill in a second application form, describing their difficult circumstances. If accepted, they are admitted with lower grades than are usually required. King's College London and the University of Southampton both offer six-year degrees (a year longer than normal) to about one in ten of their medical students. Again, only those from particular state schools or with a difficult family background are eligible. Some students may be admitted with results as low as three C grades (aspiring medics usually need straight As).

The universities are trying to correct for longstanding inequalities. Most trainee doctors come from the professional classes, and many are privately schooled.

But the academy cannot win. When A-level results were published, last August, there was a fuss about students with up to four A grades and no university places to show for them. One was rejected, without interview, by four medical schools—including King's. She, presumably, is not comforted to know that universities are trying to make two wrongs into a right.

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London's iconic offices

Love is not enough

Jan 5th 2006
From The Economist print edition

Architectural wonders are admired by all but those who sign the lease

LONDONERS love their architecture. Armed with notebooks and cameras, they swarm each September through the opened lobbies of the city's offices on a weekend-long design safari.

Above all, they love the Gherkin, as Swiss Re's 30 St Mary Axe is affectionately known. More than 13,000 building-spotters queued up on an open weekend in 2004 to visit Norman Foster's creation, which was voted the “most admired new building in the world” in a poll of architects last year.

But tenants are not showing the same level of enthusiasm. Eight of the Gherkin's 34 floors stand empty almost two years after its opening. The elegance of its pickle-shaped camber has cut its useable floor space while its stature has put off tenants who seek a lower profile.

“It's a pin-up of the London property market,” says John Forrester of DTZ, a property agent representing the Gherkin. “The only problem we've had with it is that its brand image is stronger than that of any potential tenant.”

Most tenants prefer dull, square buildings, says Chris Williams-Ellis, a director at property agents Atisreal. A case in point is the London Ark, a rotund, boat-like office building ever poised to dock with the Hammersmith Flyover.

The building attracts a steady flow of architectural pilgrims who marvel at its soaring interior and suspended walkways. It has been voted office of the year and was a runner-up in a contest to choose Britain's happiest workplace.

Pity, then, that it has stood empty for most of its 12-year life. While beautiful, the building's luscious curves limit the usable floor space and its airy atrium cuts down on privacy.

“You need great architecture and you need great design, and there is a distinction between the two,'' says Chris Hiatt, of Jones Lang Laselle. He has had more success filling competitors to the Ark than in finding tenants for it.

Box-like Plantation Place, an office block completed at the same time as the Gherkin, was fully let within months. Tower 42, the tallest building in London's old financial district and a structure widely hated before it was damaged in a 1993 Irish Republican Army bombing, is also full after a redesign added restaurants and conference rooms. The lesson: tenants prize a short walk to lunch more highly than an award-winning atrium.

This presents a quandary for developers. While function takes precedence over form in the market, Ken Livingstone, London's mayor, has made clear that tall buildings must be architecturally interesting to win planning permission. Prepare to see more elegant (and half-empty) towers on the horizon.

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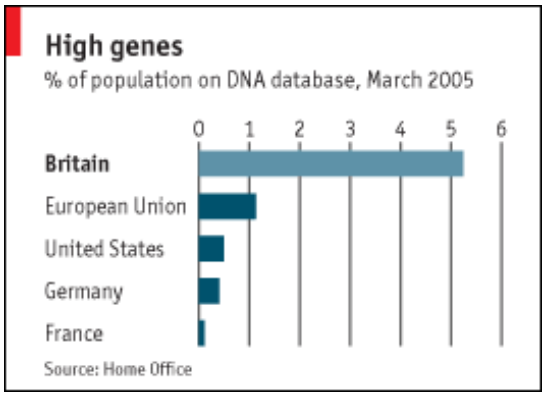
CLASSIC
PERTH 2006

DNA evidence

Biggest brother

Jan 5th 2006
From The Economist print edition

Britain's forensic DNA database is the world's biggest, and growing fast



SOME countries are more populous; some have more crime. But in no other country are crime fighters quite so knowledgeable about citizens as in Britain. On January 4th a boastful Home Office detailed the triumphs of the world's biggest forensic DNA database, which holds samples from more than 5% of the entire population of England and Wales (see chart). Recent changes to the rules governing the database mean that it may eventually hold profiles from more than a fifth of all adults.

Once a country starts storing DNA samples from criminals it is hard to resist the urge to expand the collection. When the National DNA Database (NDNAD) was set up, in 1995, samples could only be taken from those charged with “recordable” offences (those that may lead to jail terms). If a suspect was not tried, or was acquitted, the sample had to be destroyed and the profile removed from the database.

That law was ditched in 2001, after two men who had been convicted of murder and rape had their cases overturned on appeal—the DNA evidence against them related to crimes they had not been convicted of, and so ought to have been removed from the database. The change has led to the retention of around 200,000 samples that would previously have been destroyed. Some 7,591 of these were subsequently matched with samples from crime scenes, including those from 88 murders and 116 rapes. And since April 2004, police have been able to take and keep samples from anyone arrested for a recordable offence, even if charges do not ensue.

The main reason the NDNAD is larger than databases in other countries is that Britain was first to start using DNA as an investigative tool. So not only has it had time to collect more DNA samples, but it has also had longer to appreciate the sheer power of a large database. “Every other country that does databasing will get to where Britain is now,” says Chris Asplen, a consultant to law enforcement agencies and governments on DNA technology.

The increased use of DNA evidence has given rise to intriguing new courtroom defences. DNA tests are now so sensitive that they can detect if a person has sneezed or sweated near an object. Jon Swain, a barrister with a background in biochemistry, recently defended a man charged with armed robbery. The defendant's DNA was on the gun that was used, but the defence argued that he might just have been near it after he had been to the gym, and that an errant bead of sweat could account for the presence of his DNA on a weapon he had never handled. He was acquitted.

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Defence procurement

The Turner prize

Jan 5th 2006
From The Economist print edition

A national champion makes a dramatic comeback

A FEW years ago BAE Systems (which used to be plain British Aerospace until it bought GEC-Marconi in 1998) was staggering from one disaster to another. Profit warnings came thick and fast as British defence contracts ran over budget and behind schedule. As recently as February 2004, 80% of BAE business was subsidising losses made on the 20% tied up in British defence contracts.

But by then a pugnacious chief executive, Mike Turner, was taking on the bureaucrats at the Ministry of Defence. He re-negotiated contracts, refused to sign new deals until the ministry assumed some of the risk involved, and repeatedly threatened to abandon Britain for more lucrative business in America. He got his way. Contracts announced on January 4th for new armoured vehicles underline BAE's renewed status as a national champion.

BAE can now do little wrong in the eyes of the stock market or, it seems, the British government. The company's shares have tripled in the past three years. They bounced over 10% in a couple of days in December, reflecting new triumphs at home and abroad. One plum was the contract by Saudi Arabia to buy Typhoon fighters, largely made by BAE.

These are the re-branded ever-so-late, ever-so-over-budget Eurofighters made by an Anglo-German-Italian consortium. The deal, under the framework of the controversial 1980s Al Yamamah oil-for-arms contract which underpinned BAE's profits during many a lean year, indicates that this gravy train has new momentum, just when it had seemed like running into the Arabian sand.

December also saw a new defence white paper on procurement that throws out 20 years of industry bashing started by Margaret Thatcher. She brought in competition to end the cosy days of cost-plus contracts, and made the British defence equipment market the most open in the world. Whereas America buys only 9% of defence equipment from foreign sources, Britain has been buying nearly one-third.

European companies such as France's Thales, Italy's Finmeccanica and America's Boeing, Lockheed Martin and General Dynamics all have significant business with the Ministry of Defence. That could be about to change. The defence industrial strategy white paper, which helped send BAE's share price soaring in mid-December, makes it pretty clear that the concept of the national champion, sustaining technology and manufacturing capability for defence systems, is back in fashion, as it has always been on the continent and in America.

Such was the open nature of the British market that, in 1999, Thales bought Racal, a British defence electronics company, in the hope of winning juicy contracts. Now Thales and others are miffed that their investment in Britain is not being sufficiently rewarded. Only Finmeccanica is protected since it bought Westland, Britain's sole maker of helicopters, and merged it with its own Agusta business.

General Dynamics, an American maker of tanks, is said to be fuming that the white paper more or less hands BAE the role of prime contractor for Britain's new land-based combat vehicles, although Thales, Boeing and Lockheed Martin have won part of the development contracts announced this week. On the naval side, Thales has seen its hopes of dominating the contracts for two new aircraft carriers dashed. Its design will be used, but BAE will run the contract—something that seemed most unlikely only a year ago.

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Bagehot

Exciting times

Jan 5th 2006
From The Economist print edition

How good is David Cameron? How long will Tony Blair stay? Things are getting interesting

THERE'S a real whiff of excitement in the Westminster air as MPs file back after the Christmas break. The thing that British politics has been missing for a decade or more is back: suspense.

Part of it comes from the growing possibility that the Conservative Party under David Cameron really is back in business. Mr Cameron and the people around him have grasped how the party must change if it is to be a contender for office and are going about it with impressive, if sometimes opportunistic, zeal.

The growing dismay among some Tory commentators about the centrist direction in which Mr Cameron is taking the party should be music to his ears. So too should the criticism that he is substituting public relations gimmickry (the recruitment of Bob Geldof as an adviser on global poverty especially riled Tory traditionalists) for serious policy. Mr Cameron knows that there is plenty of time to think up detailed policies, but very little time for him to grab the attention of uncommitted voters and persuade them to take a fresh look at a party many had given up on.

Mr Cameron's strategy has already been rewarded by a slight opinion poll lead over Labour (a little larger if Gordon Brown is prime minister). As long as he confirms early impressions that he is a potential winner, he will have a freeish hand to go on doing the things he wants to. The most important change in the Conservative Party, symbolised by Mr Cameron's rise, is that it may at last have rediscovered its appetite for power.

Mr Cameron is also having an impact on the other two major parties. Liberal Democrat MPs, who see their seats threatened by a revived Tory party, particularly one that has learned to whistle many of their best tunes on green and social issues, are no longer willing to tolerate Charles Kennedy's inert style of leadership.

Mr Kennedy is clinging on in the hope that the cumbersome machinery for electing a new leader and the absence of an obvious replacement will rescue him. But he has lost the confidence of his closest colleagues and must soon realise that he will only inflict further damage on his party by delaying the inevitable.

Tony Blair's calculations are more complicated than Mr Kennedy's, but they too have been affected by Mr Cameron's ascent. Even more than the new Tory leader's prospects and certainly more than Mr Kennedy's fate, the question that dominates MPs' conversations is the timing of the prime minister's departure.

Mr Blair finds himself in a paradoxical position. He is full of energy and convinced that his prescription for improving public services is the only one that will work. On the other hand, the signs that power is slipping away from him are proliferating. Next week is likely to see what may well be his last cabinet reshuffle. But what should be an opportunity to shape the government for the next few years is set to be a modest affair, the high point being the probable promotion of a Blairite stalwart, Hazel Blears, from the Home Office.

Of rather more concern to Mr Blair than his dwindling opportunities for exercising patronage is the growing insurrection within the parliamentary party. Even normally quite sensible MPs, including a few self-styled New Labour modernisers, are talking quite brazenly about how they intend to derail the schools bill next month unless the prime minister gives in to their demands. Many of the same people are also threatening Mr Blair's belated attempt to encourage incapacity benefit claimants back into work, while looking for opportunities to slow down the government's NHS reforms.

Their plotting would at least be comprehensible if they believed they were doing Mr Brown's bidding and hastening the end of Mr Blair's premiership. But on this occasion, the rebels have not even received tacit encouragement from Mr Brown, nor are some of them necessarily eager for his succession. What makes it all the more astonishing is that in each case they seem happy to defy clear manifesto commitments.

Under normal Westminster rules of engagement, Mr Blair would have a straight choice between unpalatable concessions and defeat in the lobbies. However, on the “pivotal” education bill, Mr Cameron has shrewdly promised his support as long as its main thrust of giving secondary schools more autonomy is not too blunted by concessions. That gives Mr Blair a third option of making fairly trivial changes (giving statutory force to the “fair admissions” code by which schools are bound) to whittle down the size of the revolt, knowing he can depend on Tory votes to get the legislation through.

How will he jump?

Unless the rebellion crumbles (and there is not the slightest sign of that happening), whatever he opts to do, the prime minister's waning authority is certain to be further damaged. The white paper on which the schools bill will be based already represents a compromise between what Mr Blair wanted and what the powerful educational establishment could tolerate. Other than over admissions—a totemic issue for Labour that the white paper did nothing to challenge—it is difficult to see what else Mr Blair could offer up without emasculating the bill's intent. On the other hand, if around 100 Labour MPs vote against the government (nearly a third of the parliamentary party), his position would become untenable. There is no resolution to Mr Blair's dilemma.

Mr Blair wants to carry on as prime minister for at least another 18 months and possibly a bit longer. After the awful example of Margaret Thatcher, he is intent on quitting at a moment of his own choosing, ideally at a time when public service reforms have begun to take effect and British troops are beginning to withdraw from a more or less stable Iraq. And despite speculation to the contrary, he wants to hand the party over to Mr Brown in a fit state to win the next election.

But how and at what price? We should learn the answer to both those questions sooner rather than later.

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A long walk

Jan 5th 2006
From The Economist print edition

Corbis

Saudi Arabia seems a law unto itself: rich, unequal, uncompromising and unchanging. But, cautiously and almost imperceptibly, it is moving forward, says Max Rodenbeck

SAUDI ARABIA is hard to pin down. Recent book titles, strong on words such as crisis, threat, secrets and terror, seem to suggest that this is a dark and desperate place. Newspaper headlines echo the gloom with reports of bombings and shoot-outs. Opinion columns bemoan the fanaticism of its youth, the remoteness of its rulers and the power of its clerics.

Yet the latest economic reports picture a country in the prime of health where fast-unfolding reforms promise a sustained rise in living standards and an increasingly equitable spread of wealth. In the year just ended, Saudi Arabia chalked up a 7% rise in GDP, a 50% surge in oil exports and a 100% leap in prices on a stockmarket that is now worth $600 billion. Moreover, 2005 was the third successive year of similar growth. Although high oil prices clearly helped, the biggest rise was in such oil-free pursuits as finance, manufacturing and tourism, with the holy places attracting a record 6m visitors. Last year the country won admission to the World Trade Organisation. More surprisingly, it was also judged by the World Bank to have the best overall environment in the region for doing business, outperforming even such high-flyers as Dubai.

A visit to the kingdom can generate equally clashing impressions. This is a place that, infamously, chops off the hands and heads of malefactors, but its excellent hospitals also pioneer such microsurgical miracles as the separation of Siamese twins. Many people who live there, and not just the foreigners who still make up the bulk of the workforce, find the environment hostile. It is hot, parched, socially prickly, intellectually sterile, politically oppressive and legally capricious: minor infringements can lead to unpleasant encounters with roving religious enforcers. But other residents, including plenty of expatriates, love the winter sunshine, the open spaces, the easy profits and the family-oriented lifestyle. Every critic who rolls his eyeballs over excesses of religious zeal has a contented counterpart warmed by the all-encompassing faith. Each angry word about the intractability of Saudi bureaucracy or the arrogance of princes is matched by praise for the light taxes, the reassuring prudence of government policy and the generosity of ordinary Saudis.

Family secrets

If Saudi Arabia remains such a conundrum, the Saudis themselves are partly to blame. After all, the place was built and continues to be run by a family. Families like privacy, and colossally rich and conservative Muslim ones, such

as the Al Sauds, doubly so. Getting a visa to visit the country can be tricky. Subjects such as the national budget are not considered fit for close public scrutiny. Scandals tend to be swept under costly carpets.

The kingdom's Islamic conservatism is of a peculiar kind. Detractors call it Wahhabism, after the 18th-century puritan reformer whose family alliance with the Al Sauds laid the foundation for their eventual conquest of Arabia. Saudis call it Hanbalism, after a man who, a thousand years earlier, founded the most restrictive and least popular of the four accepted schools of Sunni Muslim jurisprudence. In fact, most Saudis now profess to something more of a hybrid, mixing local traditions with modern currents.

Whatever it is called, most people would agree that Saudi Islam is rigid and uncompromising, leaving a gap between ideal and practice that provokes accusations of hypocrisy. It is also self-righteous and more than a little xenophobic. The kingdom is the only country in the world, except perhaps North Korea, where the practice of all faiths but one is officially banned. Even other forms of Islam are frowned upon. That is not surprising, because other Muslims tend to regard such Saudi rules as forbidding women to drive cars or imposing the death penalty for “sorcery” as seriously backward. Pampered Saudi clerics still see relations with the wider world as a zero-sum game in which every adoption of some modern habit or gadget is seen as a loss for the purity of Islam. This breeds suspicion and mistrust—and occasional ridicule.

History, too, sets the kingdom apart. Few outsiders realise that this is one of only four Muslim countries that were never colonised by Europe, and the only one never invaded. All the others that escaped outright conquest—Turkey, Iran and Afghanistan—at various times had parts of their territory captured by “infidels”. Saudi Arabia is the site of the holiest places in Islam, which carries with it both heavy responsibilities and wide influence among the world's 1.2 billion Muslims. It is also the only modern state to have been created by holy war, or *jihad*: its present territory was captured between 1902 and 1925 by a crusading puritan army under Abdul Aziz ibn Saud, who declared himself king in 1932.

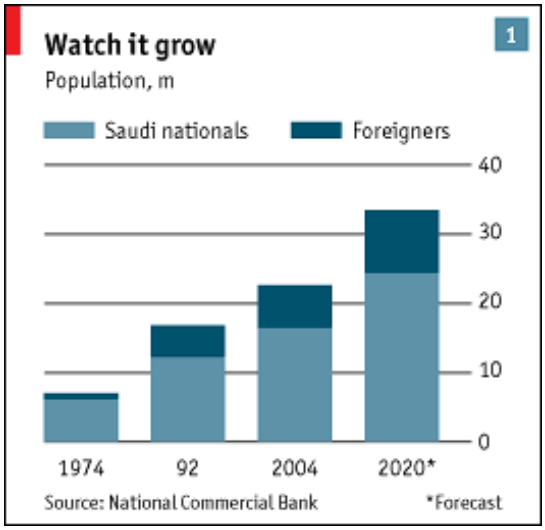
That same year, American prospectors struck oil in the east of the kingdom. But this great prize, and the avalanche of wealth it soon brought, came with unwanted consequences. One of these was security dependence on the United States, which continues to this day. Another was the mix of envy and obsequiousness (and *Schadenfreude* when things go wrong) with which other countries have treated the Saudis ever since. Oil wealth yanked a dirt-poor desert country into modernity but distorted relationships such as that between the citizen and the state, and between effort and reward in the workplace.

And then there was September 11th 2001, when 15 young Saudis helped steer several passenger planes into American landmarks. This act of mass murder thrust the kingdom into the hostile glare of global public opinion. The sheer dastardliness of the deed, and the mumbled approval of some Saudis (much to the embarrassment of the rest), brought on a bout of Saudi-bashing. The Saudis, for their part, bridled at being described in Washington as a “kernel of evil”, particularly when their own country, starting in the spring of 2003, itself began to suffer from terrorism.

All this has made an already confused picture even more confusing. Most Saudis share the West's anger and despair over violence perpetrated in the name of Islam. They admit, albeit often grudgingly, that western protection has helped save them from the failed social experiments that have plagued many other Arab countries, and that western know-how has vastly improved their lives. Yet Saudis also tend to share the radicals' perception

that their faith itself is under threat, whether from the benign influence of cultural globalisation or the malign force of what many see as American-led Crusader imperialism. Like other people, Saudis want to be modern but also to retain their identity. At present, they are torn between those who seek to “modernise” Islam and those who prefer to “Islamise” modernity.

Saudi Arabia can no longer be regarded as a simple place where an obscenely oil-rich king holds absolute sway over Bedouin subjects controlled by cash and a bleakly puritan Islam. It is now a complex, diverse and highly urbanised society, not insulated from the world but rudely exposed to it, where citizens increasingly long to be able to influence the direction of change and expect their leaders to earn legitimacy. For example, the Majlis al Shura, the kingdom's loyal, all-appointed proto-parliament, has let it be known that it will approve new taxes only if it is granted full oversight of how the money will be spent.



Twin pillars

Oil and Islam continue to define Saudi Arabia's room for manoeuvre. With global demand unlikely to wane in the foreseeable future and reserves elsewhere diminishing, oil will continue to keep the kingdom rich for decades to come. At the same time, the Saudis' attachment to their faith is not diminishing; it may even be growing stronger. But the faith itself is changing in subtle ways.

Having gone through waves of progress and retrenchment during its 73 years as a unified kingdom, Saudi Arabia is now well into another period of rapid change. This time, however, the well-oiled complacency of the previous big boom, in the 1970s, is largely gone. Four years ago, a survey in this newspaper argued that it might require internal shocks to jolt the Saudis into taking reform seriously. Those shocks have now arrived.

Since May 2003, when suicide bombers attacked a housing compound in Riyadh, terrorist violence has touched every corner of the kingdom, claiming some 200 lives. Saudi nationals, the most famous being Osama bin Laden, continue to be implicated in terrorist attacks abroad, most notably in Iraq. Yet far from rallying Saudis to the jihadist cause, terrorism has made them identify more closely with the state. More importantly, the violence has brought intense introspection and debate.

Long accustomed to blaming outside influences for all ills, Saudis now accept that the fixing needs to start at home. Aside from extremism, the problems of unemployment, poverty and the abuse of human rights have moved to the top of the national agenda. Even the most absolute of previous taboos, political reform, is being widely debated. In dozens of interviews with Saudis of all stripes, one phrase kept coming up: the question is no longer whether to reform/restructure/change, but how fast to do it.

The government's answer, to date, has been slowly, and not very surely. But this survey will argue that far from being a dinosaur nation, lumbering to extinction, Saudi Arabia is capable of rapid evolution. On some important issues, such as the rules governing business, it is already far down the right track. On others, such as the ways it educates its youth and excludes women, the kingdom is only just beginning to shift course. What has been sorely lacking is a firm hand at the wheel.

Such leadership could come from the Al Sauds themselves. The assumption of the throne last year by King Abdullah, who has embraced greater openness than his predecessor, has raised hopes. The new king is personally far more popular than the previous one. Yet reforms would undoubtedly be more effective if they were backed by a clear popular mandate. Most Saudis reckon it is premature to speak of democracy in their country; but there are myriad ways to emancipate citizens, from upholding the rule of law to making budgets more transparent and loosening the grip of security agencies over universities and the press. Instead of their old tactics of prevarication, slow consensus-building and co-optation, the Al Sauds should try a new one: putting trust in their people.

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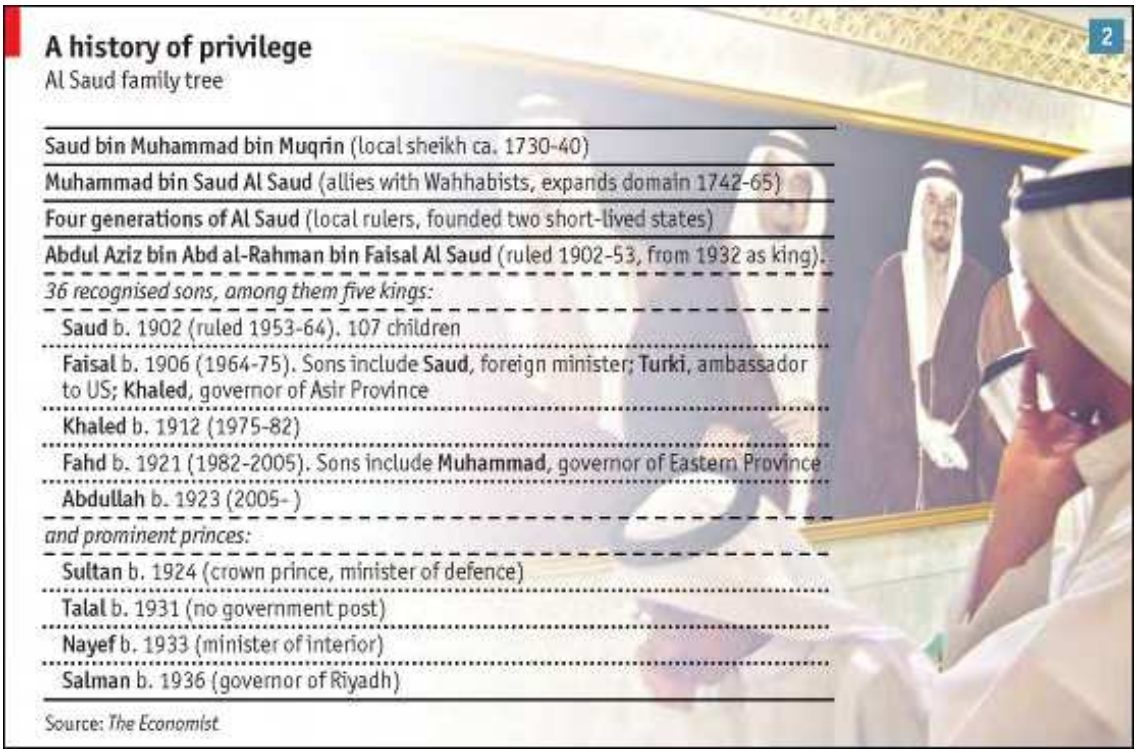
All in the family

Jan 5th 2006
From The Economist print edition

The Al Sauds run everything

IMAGINE that Britain was known as Windsor Britannia, or Spain as Bourbon Iberia; that their royal families still ruled directly, with no messy elected bodies in the way; and that their members included not just the royal couple, some wayward kids and a few cousins, but thousands of princelings, all demanding grace and favour. Imagine, further, that every newspaper felt obliged to print such choice items as this: “The Custodian of the Two Holy Mosques, King Abdullah bin Abdul Aziz, has sent a reply cable of thanks to Crown Prince Sultan bin Abdul Aziz, Deputy Premier, Minister of Defence and Aviation and Inspector-General, thanking the Crown Prince and all personnel of the armed forces for their congratulations to the King on the occasion of Eid al Fitr, marking the end of the holy month of Ramadan, in the cable sent earlier to the King by the Crown Prince.” Surely a text message would have done.

AFP


A history of privilege
Al Saud family tree
2
Saud bin Muhammad bin Muqrin (local sheikh ca. 1730-40)
Muhammad bin Saud Al Saud (allies with Wahhabists, expands domain 1742-65)
Four generations of Al Saud (local rulers, founded two short-lived states)
Abdul Aziz bin Abd al-Rahman bin Faisal Al Saud (ruled 1902-53, from 1932 as king).
36 recognised sons, among them five kings:
Saud b. 1902 (ruled 1953-64). 107 children
Faisal b. 1906 (1964-75). Sons include Saud, foreign minister; Turki, ambassador to US; Khaled, governor of Asir Province
Khaled b. 1912 (1975-82)
Fahd b. 1921 (1982-2005). Sons include Muhammad, governor of Eastern Province
Abdullah b. 1923 (2005-)
and prominent princes:
Sultan b. 1924 (crown prince, minister of defence)
Talal b. 1931 (no government post)
Nayef b. 1933 (minister of interior)
Salman b. 1936 (governor of Riyadh)
Source: The Economist

Apologists describe Saudi *majlises*, those public receptions where princes listen to their subjects' pleas and panegyrics, as a form of “desert democracy”. In fact, they are stilted, staged affairs. Prince Waleed bin Talal, the king's nephew, is renowned for the charity dispensed at his weekly *majlis*. Yet the billionaire investor pays scant attention to the hundreds of supplicants who shuffle forward for a perfunctory hearing, after which an aide often hands them an envelope of cash.

The surprising thing is how comfortable most Saudis seem to be with their ruling dynasty. Testy regionalism persists, for instance, among the Shia of the Gulf coast and the Ismailis along the border with Yemen, as well as among the proud old families of the Hijaz, the relatively cosmopolitan region around Mecca. But although its advocates would like more rights and less Wahhabism, they do not question the legitimacy of the Al Sauds.

King and country

One reason for this is that most Saudis have done pretty well under the family's rule. The kingdom's social peace may come at a high cost in personal freedom, but it compares well with the unrest in nearby countries. For all the talk of mismanagement and waste, Saudi Arabia has a decent infrastructure and some fairly efficient institutions. “In some autocratic regimes there is no good intention to improve things,” says one junior prince. “Here there was always a good intent, only the tools were sometimes weak.”

Besides, Saudis know that their country would not exist without the Al Sauds. Until the 20th century, there had never been a state that covered similar territory. The prized Hijaz fell under the sway, successively, of rulers in Damascus, Baghdad, Cairo and Istanbul, who ignored the Arabian interior, or Najd, as worthless. King Abdul Aziz, the current king's father, built his kingdom through a mix of outright conquest, appeals to the faithful, strategic marriage and clever diplomacy. He and his heirs sustained it by carefully cultivating tribal, business and religious leaders and through the wildly generous patronage made possible by oil wealth.

The sheer size of the Al Saud clan has also helped cement the nation. There have been eight generations of Saudi rulers, dating back to 18th-century sheikhs who held sway in a few oasis towns near present-day Riyadh. Many have been prolific. King Abdul Aziz himself sired some 36 sons and even more daughters. The first son to succeed him, King Saud, fathered 107 children. King Abdullah is believed to have 20 daughters and 14 sons. The extended Al Saud family is now thought to number some 30,000, though only 7,000 or so are princes. Of these, only around 500 are in government, and only perhaps 60 carry real weight in decision-making.

Aside from controlling positions directly, the Al Sauds exert continued influence through marriages with such respectable Najdi families as the Al al-Sheikh, who are descendants of the founder of Wahhabism. Many princes still surround themselves with traditional retainers knows as *khuyas*, or “little brothers”, who typically represent Bedouin tribes. Tribal links are also maintained through selective manning of such institutions as the Saudi National Guard.

Such layers of influence have proved gratifyingly coup-proof, but the real clincher has been the perpetual fountain of oil wealth. Forty years ago King Faisal, the great reformer and moderniser, having ousted his profligate brother Saud, decreed that the royal family's take from oil exports should be capped at 18%. That rule probably still applies today, though it is hard to tell because the state budget remains opaque. The current king, Abdullah, is known to frown on extravagance; he likes desert rambles in his specially fitted bus, whereas King Fahd liked flying his entire court to his holiday palace in Spain's Marbella. No doubt, however, the Al Sauds are still comfortably off. Even lowly princes are believed to receive a monthly stipend of at least $10,000. The combined wealth of the Al Sauds is impossible to guess, but it must be hundreds of billions of dollars.

Commoners do complain about undue spoils, but money on such a scale also buys consent. Al Sauds and their loyalists control all of the dozen Saudi daily newspapers. They own the two most respected pan-Arab dailies, as well as four out of five of the most popular Arab satellite TV channels. The exception is al-Jazeera, which is one reason why the cocky channel is subject to a ruinous boycott by Saudi advertisers. Aside from keeping top western lobbying firms on their payroll, the Al Sauds can also flatter influential Muslims by offering them privileged access to the crowded holy sites. “Their money turns lies into truth,” says one human-rights activist.

Caesar, thou art mortal

Yet Saudi kings, despite the lack of constitutional constraints on them, are far from absolute rulers. They have, first of all, to account to the Wahhabist religious establishment that has been their traditional legitimation. This can be a serious handicap. King Fahd, who ruled from 1982 until last August, is said to have lavished favour on religious causes to atone for his own youthful reputation for high living. And although kings appoint senior members of the clergy, they have no direct oversight of the 700 judges who run the *sharia* courts, the backbone of the Saudi legal system and the bane of reformers.

The king must also answer to his own enormous family. By tradition, succession is not vertical, passing to sons, but horizontal, passing to brothers in order of age or, sometimes, merit. During the 52 years since the death of the kingdom's founder, many of his sons, of whom a dozen are still in line for possible succession, have used their long wait to create powerful fiefs. Prince Salman, now 69, has been governor of Riyadh since 1962. His full brothers include Sultan, the 81-year-old crown prince, who has been minister of defence since 1962, and Prince Nayef, minister of the interior since 1975. All have appointed their own sons to top posts.

It is often claimed that these full brothers, called Sudairis after the family name of their joint mother, have stood in opposition to other princes. As crown prince, for example, Abdullah, who has no full brothers, was forced into some humiliating retreats from initiatives he had sponsored, even after the 1995 stroke that incapacitated King Fahd (another Sudairi) and left Abdullah supposedly in charge. But some analysts identify at least five competing spheres of power within the ruling family. This, it is said, explains the sometimes erratic course of Saudi policy,

with reforms being promised and then retracted. Elections to municipal councils, for instance, were first mooted in the 1970s, but held only last year, and then only for half the seats.

Certainly Abdullah, aged 82, appears to have more leeway now that he is king. So far he has pointedly refrained from the customary naming of a second deputy prime minister. This is the traditional post for a runner-up to the throne. Crown Prince Sultan held that position under Fahd, and is now first deputy prime minister. This has been read as an oblique signal of discomfort at the prospect of power passing to Prince Nayef after Sultan. The 72-year-old interior minister is the most prominent, though not the most senior, contender, but he is widely regarded as moody, abrasive, capricious and prone to intrigue. The king's appointment of Prince Bandar bin Sultan, the flamboyant former ambassador to Washington, as head of a more powerful National Security Council is seen as trimming Nayef's sails further.

King Abdullah has taken other small steps to boost his already considerable popularity. One of his first acts in office was to free three prominent dissidents, whose jailing, for the crime of calling for a constitutional monarchy, had sent a chill through reformist circles. Soon after, Abdullah decreed that the kingdom's little-observed National Day should become a public holiday. Conservative clerics complained of creeping secularism, but ordinary Saudis loved it. The king also decided that no one should kiss his hand any more.

Such gestures reflect Abdullah's own attachment to Bedouin egalitarianism, but also an awareness that times are changing. Since the reign of King Faisal, who was murdered in 1975 by a disgruntled nephew, the Al Sauds have suffered a steady loss of public goodwill. One symptom of this has been the presentation of citizens' petitions demanding reform, a trend that began in 1990 and reached its height in 2003 before a crackdown in the last year of King Fahd's reign. Although the Al Sauds' response to such polite prodding has been outwardly muted, many of the reforms undertaken in the past 15 years have been aimed at meeting petitioners' demands. In 1992, King Fahd decreed a basic law that for the first time outlined an institutional structure for the state. (Saudi Arabia has no constitution, claiming that the Koran serves this function.)

King Fahd also created the Majlis al-Shura, or consultative council, which has since expanded to 150 members. It is easy to dismiss this all-appointed body as window-dressing, but even detractors admit that its legislative record is good, and its membership broadly representative of the kingdom's diversity (with the huge proviso that it excludes women). Senior princes speak of elections to at least some Shura seats in the future. Already, prominent members have called for greater power to grill officials and authorise budgets, and even talked about launching public debates on controversial issues.

Such gradual progress goes some way towards appeasing the many Saudis who would like to see a fuller devolution of autocratic powers. Many of them claim to be untroubled by another issue that will affect the country's political future: the succession. Both King Abdullah and his designated heir are old men, but the general assumption is that the Al Sauds are not yet ready to see power pass to the next generation, King Abdul Aziz's grandsons. Many suspect that the brothers of the ruling generation could not agree on whose son should get the prize.

Clearly it would be good for the country to have a younger, more dynamic king, or at least a clearer mechanism for transferring power. For the time being, though, Saudis will just have to wait. One young prince, Muhammad bin Abdullah al-Faisal, who runs one of the kingdom's largest private firms, the Faisaliah Group, finds the political arena overcrowded, but thinks the family will sort something out. “The floor that stops me feeling uncomfortable is that there is no one in the line of succession who wants to go down in history as the one who lost the kingdom.”

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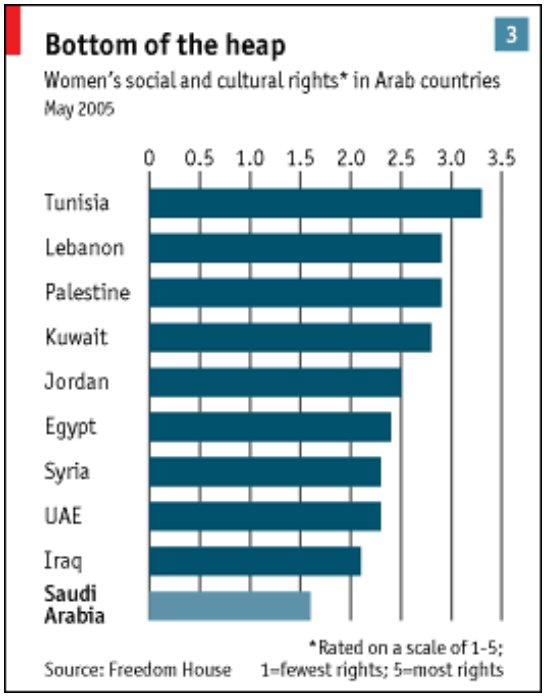
Glacier in the desert

Jan 5th 2006
From The Economist print edition

Ever so slowly, Saudi society is moving forward

THE National Commercial Bank, the kingdom's oldest and biggest, is running an advertising campaign. One slick television spot features a smiling young woman showing her delighted father how to settle bills by direct debit. The same ad could have run anywhere (though perhaps without the headscarf for the dutiful daughter). But in a country where until a few years ago women did not appear on TV at all, and until the 1960s did not even go to school, there is a subversive significance to suggesting that a woman can be more savvy than a man, and that the old can learn from the young. Formally, the kingdom's women remain the most oppressed on earth. They are, famously, barred from driving, and this in a steamy land with sprawling cities. It is not merely humiliating to be at the mercy of male relatives, who need cajoling or sometimes bribing to get behind the wheel. It can be crippling, even for wealthy women who can afford drivers. One mother of a two-year-old describes her rising panic when her son fell ill while her husband was travelling, and her driver failed to show up for several days because he had wrecked her car for the third time.

Yet few women see driving as a priority for reform. Not even the Wahhabist obsession with preventing *ikhtilat*, or "mixing" of the sexes, comes near the top of many Saudis' long wish list for change. This may sound odd to visitors, for whom the most striking aspect of Saudi life is the effort to separate the sexes entirely, not only in schools and universities but also in offices, restaurants and even banks. So successful is the effort that, aside from private homes, the most uninhibited spaces in today's Saudi Arabia are the holy cities of Mecca and Medina: less prudish foreign Muslims mingle freely here, and statutory pilgrim garb is actually more revealing than the cover-all black *abaya* required in other Saudi cities.



In fact, a surprising number of Saudi women are quite content with the ban on *ikhtilat*. Some of them are more bothered by the incompleteness of the separation. Many government departments, for instance, have failed to create a women's section, so women either have to send an appointed male agent or be accompanied by a *mahram* or protector: a father, husband, brother or son.

This is what really riles even the most pious of Saudi women. They may accept, on scriptural grounds, that a woman is worth only half a man's share in inheritance, in blood-money and in the weight of her testimony in court. But most of them object to the general infantilisation of women, which has no basis in Islam. Successful female entrepreneurs—and there are many in the kingdom—resent having to appoint male agents to represent them. And even happy housewives know that their husbands can, if they choose, deny them the right to travel, work, or study at university. Should a marriage go sour, mothers have no right to custody of the children. Men may divorce their wives with a simple oath, but women must plead with the all-male, all-Wahhabist judiciary to divorce their husbands.

What women really want

Even some feminists, however, say there are more pressing issues. "Just give us all, men and women, free speech and the right to organise," says one Riyadh activist. "All else will follow." Ibrahim al-Mugaiteeb, one of the country's most tireless human-rights campaigners, reckons that although such formerly common abuses as torture in prisons have lessened, nasty practices such as arbitrary arrest, imprisonment without trial and being denied access to a lawyer continue. Like scores of others, Mr Mugaiteeb is himself banned from travel outside the

kingdom, and harassed by frequent summonses for questioning by police. Millions of immigrant workers, he says, face constant petty discrimination and have little recourse to justice. Household servants are often kept in slave-like conditions. Persecution of religious minorities, including non-Wahhabi Muslims as well as visiting Christians, continues.

Activists from the 200,000-strong Ismaili Shia community in the remote province of Najran, for instance, complain of gross under-representation in all branches of government, the deliberate settling of Sunni Bedouins in the region, and ritual humiliation in courts and schools that are uniformly run by Wahhabists. In one particularly odd case, a Najran judge sentenced a 16-year-old Ismaili schoolboy to death for blasphemy. This was commuted on appeal to 14 years in prison and 4,000 lashes, to be administered publicly in 80 weekly sessions of 50 blows.

Most Saudis are unaware of such injustices. A poll conducted in 2004 found that the issue which concerned them most, more than religious extremism or women's rights, was unemployment. This is certainly a big problem. Official figures put the rate at 9.6%. Outside estimates suggest it may be as high as 20%, but it is hard to tell because many Saudis of working age, including nine out of ten women, are not actively seeking jobs. What is clear is that the problem has grown rapidly.

Part of the reason is that with half its people under the age of 20, the kingdom is having to cope with a big population bulge. More importantly, though, government statistics show that despite 20 years of official efforts to “Saudise” the workplace, foreigners still make up 60% of the 8.5m-strong workforce, and a much higher proportion of those employed by private businesses. Saudis are averse to taking orders or work they see as demeaning, and imported labour is, on average, 30% cheaper than Saudi manpower. Private employers have such a strong preference for foreigners that many resort to creating pretend jobs for Saudis to meet increasingly tough quotas. A law just passed that requires 75% “Saudisation” simply cannot be complied with in the short term, says one experienced consultant.

The underlying obstacle to getting Saudis to work is that schools are not producing employable people. This is due partly to the weight put on religious instruction and partly to the emphasis on rote learning. The offputtingly dull curriculum may explain, for example, why a survey of Riyadh high-school students found that fewer than one in six did any reading for pleasure. Absolute separation of the sexes creates obvious inefficiencies, too, especially in universities (where women, incidentally, make up 55% of all students). And most of the degrees granted are in theoretical subjects, such as theology.

Even so, economic pressures have pushed growing numbers of Saudis into jobs that their parents would have disdained. It is no longer odd to see Saudi clerks, receptionists or salespeople. “I know guys who are making just 1,500 riyals a month ($400), with terrible working hours,” says Pascal Ménoret, a French academic who has spent years studying the kingdom. “You can barely live on that, and there's no hope of saving for marriage.”

Something to do

A more common hazard of Saudi life is harder to measure: simple boredom. The bans on mixing, as well as on public entertainment such as cinemas and theatres, leave few distractions beyond home, family and the mosque. Many Saudis have grown addicted to satellite TV. Sociologists also note an increase in *tafheet*, juvenile delinquency such as drug-taking, hooliganism and late-night drag-racing in city streets. Boredom also prompts some to turn to religious extremism.

The rest make do with shopping. When a new store in Jeddah handed out gift vouchers to promote its opening last year, 15,000 people turned up, creating a stampede in which two people got trampled to death. What attracted them, said a local columnist, was the utter lack of anything else to do.

AP

Cataloguing such social ills is something of a Saudi national sport. Yet whereas complaints used to be whispered behind closed doors, they are now increasingly aired. The Saudi press has gone through phases of daring and cowardliness in turn, depending on the government's mood, but in general it is more professional and reflects public concerns more accurately than in most other Arab countries. The recent intrusion of other media that are immune from princely threats, such as internet chatrooms and mobile-phone messaging, has made Saudis far more aware and engaged with their surroundings than they used to be.

Public exposure of scandals has not only widened the range of permissible debate, it has increasingly prompted a healthy search for practical solutions. A school fire in 2002 that killed 15 girls, whom religious police were reported to

have stopped from fleeing the building unveiled, led to the sacking of the Wahhabist head of girls' education and the department's absorption into the education ministry. In 2004, a popular TV presenter, Rania al-Baz, took the unprecedented step of inviting reporters to photograph her shattered and bruised face after a savage beating by her husband. The outcry helped silence conservative critics of several subsequent reforms, including laws granting women the right to ID cards. More recent exposés have revealed such things as inhumane treatment of mental patients and the sexual harassment of women.

A woman's lot

A different kind of scandal erupted two years ago when Lubna Olayan, a rich businesswoman who heads a 40-firm conglomerate, failed to notice as her headscarf slipped during her opening address at a business event in Jeddah, prompting a thunderous warning against such corruption and depravity from the kingdom's most senior cleric. The conservatives seemed to have won that round. The government said nothing. But this autumn, when it backed a move to let women vote and run in elections for the board of the Jeddah Chamber of Commerce, there was not a peep of clerical complaint.

“People who oppose modernism shout a lot,” says Madawi Hassoun, an enthusiastic candidate for the board. “But if you deliver results, they stay quiet.” Ms Hassoun, who runs a string of beauty parlours and home-accessories shops, believes that change is inevitable. Even so, she sees wisdom in the government's slow, consensual approach.

In such halting, roundabout ways, the agenda of social reform slowly progresses. Even the touchstone issue of women driving is no longer taboo. Opinion polls show that a majority of Saudis think it should be allowed, and also that a third of women already know how to drive. King Abdullah's own daughter, Princess Adila, was recently quoted as saying that giving them licences was only a matter of time.

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Keeping the faith

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A very special kind of Islam

UNTIL two years ago, Saudi religious textbooks suggested that a good way to show love for God was to treat infidels with contempt. Students learned that communism, secularism and capitalism were forms of apostasy. Inventors and those who call themselves scientists, they read, were nothing of the kind because their so-called science was limited to worldly matters. The only true men of science were those who knew God and feared Him.

Passages such as these have since been purged, as part of a general campaign against "exaggeration" in religious teaching, but not without fierce resistance. In 2004, for instance, a group of 150 religious scholars, among them officials in the education ministry, blasted such revisionism in a petition. "It is not possible to erase this enmity simply by removing something from the curriculum!" exclaimed their message to the king. "The enmity between infidels and Muslims is a fact of existence as well as a legal obligation."

AP

Home truths

Many teachers have simply refused to use the kinder, gentler new texts. Even some parents complain that they no longer trust the curriculum to convey correct values. In one notorious incident last year, colleagues and students of a high-school chemistry teacher pressed charges against him for speaking against jihadist violence, for "favouring Christians and Jews", and for poking fun at clerics' beards. The local judge handed him a 40-month jail sentence, plus 750 lashes.

Texts containing incitement to religious hatred are still stocked in mosques, bookstores and libraries. A giant state-run press outside Medina, for instance, produces some 10m beautifully printed Korans a year, in 40 languages, which are distributed free throughout the world. Yet these are no ordinary Korans. They are annotated by Wahhabist scholars, who pronounce, among other things, that *jihad* is one of the "pillars" of Islam. (Most Muslims recognise five pillars: the profession of faith, prayer, alms-giving, fasting and pilgrimage.) "By abandoning *jihad*, Islam is destroyed," says one footnote. "*Jihad* is an obligatory duty, and he who tries to escape this duty, or does not in his innermost heart wish to fulfill this duty, dies with the qualities of a hypocrite."

Obviously, most Saudis make their way through life without taking up arms against the world. But plenty do feel inspired by such fighting words. In the past, and often with a nod from Washington, the most enthusiastic were exported to such theatres of war as Afghanistan, Chechnya and Bosnia. Some estimates put the number of Saudi volunteers in those conflicts as high as 30,000. Generous funding also flowed to jihadist causes, often without the knowledge of the donors. ("I thought it was like the Salvation Army," says a Riyadh businessman of a charity he had long sponsored before it was linked to terrorism.) The skies of America, as well as Iraq, have been more recent arenas for youths wishing to sacrifice their lives for what they see as the good of the faith.

Whatever their reservations about jihadist tactics, most Saudis were impressed by their zeal and at least somewhat sympathetic to their goals. Television pictures of Muslims suffering injustice in Palestine and elsewhere bolstered the already xenophobic world view of the Wahhabist establishment that controls the kingdom's mosques and schools. After September 11th 2001, America's proclamation of war on terror, accompanied by words and phrases such as "crusade" and "with us or against us", fed suspicions of a plan to divide and weaken Muslims.

Not in our backyard

But such defensive complacency came to an abrupt end in May 2003 when a local cell linked to al-Qaeda sent

suicide truck bombs into three residential compounds in Riyadh. The following 18 months saw a series of deadly bombings and shoot-outs as militants attacked expatriate workers as well as Saudi police. The security forces' response at first seemed bungling and confused, but slowly they gained the upper hand. There have been no significant attacks since December 2004.

The killing of scores of suspects and the arrest of hundreds more is one reason for the decline in violence, but psychological attrition may have been more effective still. Ordinary Saudis have been outraged by the militants' callousness, and disturbed to see their safe, quiet cities rattled by gunfire. Even outright bigots have found it hard to excuse the radicals' taking of Muslim lives. The authorities have capitalised on such feelings by showing emotive footage of weeping mothers and fathers denouncing their jihadist sons. A senior prince in the security forces reckons that 80% of their success is due to such persuasion and only 20% to better policing.

More significantly still, the bloodshed has prompted inquiry into its root causes. Some of these are historical. Before the creation of the Saudi state, the majority of people in the future kingdom's territory did not follow the Wahhabists' Hanbali school of Islam. The great mosques of Mecca and Medina were famed for the diversity of the scholars who taught there. This liberal stance incensed the Al Sauds' puritan Bedouin warriors. Yet once he had captured the holy cities, in 1925, Abdul Aziz Al Saud began to bridle at his allies' fanaticism. They alienated his subjects by such actions as destroying the tomb-shrines of the Prophet's descendants, which they said were objects of idol-worship. The Wahhabi ranks split and senior clerics sided with the Al Sauds, arguing that obedience to a “rightful commander” was preferable to anarchy. Some joined jihadist rebels who denounced the Al Sauds for going soft. The rebels were eventually crushed, but the conflict underlined the Saudi rulers' dependence on loyal Wahhabist clerics.

Ever since, Saudi rulers have been careful to maintain this loyalty, taking out what the French Islamologist Gilles Kepel calls “ideological insurance”. Clerical approval was always sought, and sometimes obtained only with great difficulty, before reforms such as the introduction of banking and paper money in the 1950s and the abolition of slavery and the start of schooling for girls in the 1960s. When television arrived in 1965 it caused riots, quelled only when senior clerics grasped the fact that they could use this heathen innovation to promote the faith. In 1979, after a band of messianic Wahhabist radicals invaded the great mosque at Mecca, loyal clerics gave their blessing to the use of firearms to flush them out. Perhaps most controversially, in 1990 they gave grudging approval to the deployment of American troops on Saudi soil to repel Iraq's invasion of Kuwait.

The clerics' loyalty stretched to overlooking other things that might have been criticised on religious grounds, such as royal corruption, as well as many practical secular innovations. Saudi banks, for instance, have been offering interest-bearing accounts right from the start, despite Islam's reservations about interest. The highly regarded central bank simply argued that the banks' clients should be allowed to choose the kinds of financial instruments they wished to use. Commercial disputes have not been settled in *sharia* courts since the 1960s because their rulings were found to be ruinously unpredictable. Instead, such disputes are referred to a commission appointed by the Ministry of Trade.

The Al Sauds rewarded the clerics' loyalty well. Wahhabists were given full control of criminal and personal justice and extensive influence over education. Wahhabist schools and *sharia* courts supplanted older institutions across the kingdom. The powers of the *mutawaa* or religious police were widened, and rules on such things as female dress more rigidly enforced. Huge sums went to religious causes, from the founding of Islamic universities to the building of mosques and the expansion of pilgrimage facilities. In the 1980s funding was increased further by King Fahd, who wanted to bury his previous reputation for moral laxity but also saw a threat to the kingdom's primacy among Muslims from revolutionary Iran.

But the clerics' loyalty came at a cost. Students in the new institutions began to question the scriptural basis for their support of the Al Sauds and their policies. Some turned to the ultra-puritan ideas of earlier Wahhabist rebels, but the lavish state patronage also attracted foreigners, who brought with them new ideological currents and a modern take on Islamic governance. Thousands of Muslim Brothers, persecuted in Egypt and Syria, found refuge in the kingdom. They included Muhammad Qutb, whose better-known brother, Sayyid Qutb, was hanged in Egypt for teaching that *jihad* must be waged against Muslim rulers who stray from Islam. Muhammad Qutb taught for years at Mecca's Umm al Qura University. His ardent followers included Osama bin Laden, his deputy Ayman al-Zawahiri and the populist Saudi preacher Safar Hawali.

The 1970s and 80s saw the quiet emergence of a youthful counter-movement to official Wahhabism. Known as the *sahwa*, or awakening, it came into sudden full view during the 1990-91 Gulf crisis. Preachers such as Mr Hawali gained instant prestige from their opposition to the alliance with infidel America and their demands for political reform within a new model of an Islamic state. Their outspoken views inspired a wave of activism, including attacks on shops selling videos and satellite dishes. In a crackdown in the mid-1990s, many young activists were imprisoned or fled abroad. The heavy-handed response pushed some activists, such as Mr bin Laden and his followers, towards terrorism, and the Al Sauds themselves became a prime target.

A symbiosis challenged

“The Wahhabi-Saudi alliance worked like magic,” says a liberal lawyer in Riyadh. “But now it's turned against the magician.” However, that may be too simple a view. The large official religious establishment, paid for by the state, is ostensibly made up of loyal Wahhabists. Some of them, including nearly all the kingdom's 700 judges, are extremely conservative. The country's main universities also remain steeped in Wahhabist thought. But the Wahhabists' religious rulings have lost credibility with the wider public. Their official condemnation of terrorism, for example, is based mainly on the argument that it represents disobedience to the “rightful commander” under whose sole authority *jihad* can be pursued.

Many Saudis, particularly junior bureaucrats and schoolteachers, look instead to the activist Islamism of the *sahwa* and the Muslim Brotherhood. It, too, is conservative and xenophobic, but its attitude to the role of the monarchy is more questioning and its approach to social issues slightly more progressive. To its supporters, al-Qaeda-style violence is an aberration in itself, although “resistance” in Iraq or Palestine is perfectly legitimate. It was this movement, which some call *Islahi* or reformist, that performed best in last year's partial municipal elections.

Some charged *Islahi* candidates with using scare tactics, such as accusing liberal rivals of secularism, which Saudis consider a vicious slander. But Bassim Alim, a Jeddah lawyer with a Harvard degree, thinks the *Islahi* movement was simply better organised. “Many people felt like me,” he says. “The elections were an opportunity to send a message that we are a Muslim country. You could say we are fundamentalists, but not fanatics. I want my country to be Islamically inclined, but with an open mind. Right now, the use of Islam by the Saudi government is much like the way communism is used by the Chinese, just to control people.” Mr Alim has taught his daughters to drive, and would be “ecstatic to have American-style democracy or any kind of democracy”. But he describes America as a racially bigoted country bent on world domination.

A small but increasingly vocal group of Saudis takes a much more liberal view of religion and state. This progressive elite is poorly organised, as its trouncing in the election showed, and Islamists, even modernist ones such as Mr Alim, say it is out of touch with the pulse of Saudi society. Yet it has a strong voice, both in the local Saudi press and on the satellite channels that are the kingdom's main source of information and entertainment. “I don't want revolution, and I think most Saudis believe democracy is pie in the sky,” says a cigar-chomping stockbroker. “But I want the interior and justice ministries purged, and the whole question of who appoints judges revised.”

The Al Saud family itself represents a broad spectrum of opinion. King Abdullah, for example, is a traditional, pious conservative, but quietly backs a more liberal social agenda. “He feels betrayed by the religious establishment,” says a history professor in Riyadh. “He thinks they created the environment that made terrorism possible.” But although many younger princes would like to see a full break with the Wahhabist alliance, senior princes remain fearful of radical action. One very wealthy member of the royal family, himself a liberal, says he still prefers to buy “immunity” from conservative criticism by handing out generous charitable donations.

To date, the Al Sauds seem to have tried to preserve a balance. They have silenced liberal demands when they have grown too strident; yet in the past few years they have also got the most fanatical preachers sacked, school curricula revised and religious tolerance vigorously promoted. “Until two years ago the *mutawaa* could say anything they like, they could not be challenged,” explains Prince Waleed bin Talal, who is both actively pious and an outspoken defender of women's rights. “Now they are being handcuffed, but gently, because when you fight them with logic they prove to be weak.” He adds with a mischievous grin: “I like it when they bark. It means they're in a corner.”

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A Mecca for money

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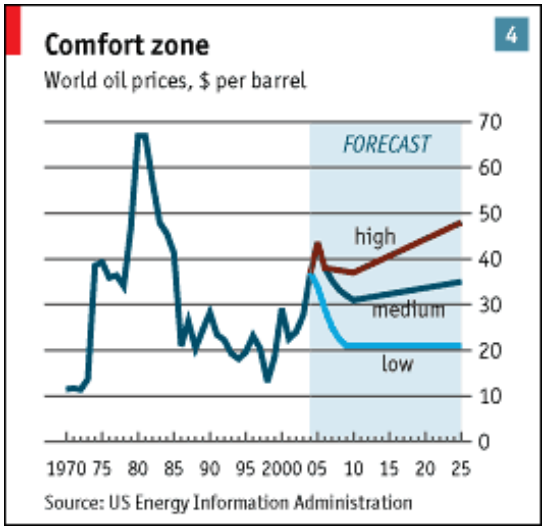
From The Economist print edition

The economy is doing almost too well for its own good

RUMOURS, whether true or not, can tell you much about the mood of a place. One story whispered around Riyadh concerns a prominent businessman who spoke loudly and often about the astonishing progress being made in Dubai. It was a shame, he said, that Saudi Arabia was slow to follow the nearby emirate's freewheeling style of business. A senior prince summoned the man to hear all about it. When the businessman had finished, the prince slapped him hard on the cheek and said, “Don't speak of Dubai again.”

It may be nothing more than a good story, but it says much about the issues on Saudi minds. For all the kingdom's wealth, even the oil windfall of the past few years has raised its income per person only from the level of Mexico to that of Argentina. A quarter of a century ago it was, albeit briefly, on a par with America's. For most of the time since then, flat oil prices have kept the pie from getting much bigger but rapid population growth has meant it had to be divided up into many more pieces.



Citizens of some smaller Gulf emirates, by contrast, have come to enjoy a standard of living closer to that of Luxembourg or Monaco. Multinationals that flock to invest there have largely shied away from the kingdom with its stricter laws and even stricter rules of personal behaviour. Saudis themselves travel a lot and invest heavily in the rest of the Gulf. A recent share offering in the United Arab Emirates sent 30,000 of them scuttling next door to place bids, causing the petrol station at the border to run out of fuel. The IPO was 222 times oversubscribed.

Nice big earner

But the Saudi punters' interest in their neighbour does not signal weakness in their own economy. Oil exports, having bottomed out in 1998 at $35 billion, have since soared, hitting a record $160 billion in 2005. Last year's current-account surplus was close to $100 billion and the central bank's net foreign reserves rose to $135 billion, a jump of $90 billion in just three years. Last August the government granted a 15% across-the-board pay rise to its employees, the first in 22 years. Though consumer inflation remains very low, the influx of cash has sent asset prices soaring. The Riyadh stock index has quadrupled in just two years. Prime building land in Mecca now fetches close to $100,000 a square metre ($9,300 a square foot).

Even better, oil prices are likely to remain strong. True, in the past six months they have drifted downwards from last year's spike, and forecasts are notoriously risky. But America's Energy Department, whose data-crunching is well respected, has recently adjusted its medium-term scenario from the present to 2025, suggesting that oil prices during this period could on average be around 50% higher than in the previous 20 years, and rising.

That would be very comfortable for the Saudis. Since the 1970s, they have been wary of prices rising to the point where rivals would be encouraged to exploit oil fields that had previously been uneconomic. Saudi oil costs just $2 a barrel to produce, a small fraction of what it costs to extract the stuff in Alaska, say, or the North Sea. Demand from both Asia and America remains strong. Saudi Aramco, the giant state oil monopoly, is ramping up its production capacity. Having remained static at around 10m barrels per day for a generation, this is currently pushing 11m and may reach 12.5m by 2009 and perhaps 15m by 2015. Assuming a middle-of-the-range price of around $40 a barrel, the oil bubbling out of the ground could continue to be worth around $500m a day for many years to come.

Yet it is not just the world's thirst for oil that justifies Saudi optimism. In the first three quarters of 2005, for instance, the kingdom's 11 banks raked in combined profits of $5 billion, $1 billion more than for the whole of 2004, which

itself was a vintage year. This is not bad for a $300 billion economy. Corporate lending has increased by half in the same two years, and overall loan-to-deposit ratios rose from a limp 64% to a sounder 80%. In other words, banks are not just accumulating deposits or funding the stock frenzy, but pumping capital into productive investment.

Other industries are doing nicely too. Take SABIC, a maker of petrochemicals and steel and the Middle East's largest industrial group. Twenty years ago it hired an American consulting firm to gauge its long-term prospects. The same consultants reckon that SABIC is now 70% bigger than they had predicted back in the 1980s. It currently makes 7% of the world's petrochemicals, a figure it expects to rise to 13% by 2010. The company doubled its profits between 2003 and 2004, and increased them by a further 54% in the first nine months of 2005, to an enviable $3.9 billion on sales of $15 billion. SABIC's stockmarket value has grown to a whopping $175 billion.

Nor is the company alone in being so successful. Dozens of Saudi firms have expanded similarly, and can hold their own against the world's most competitive enterprises. Non-oil exports were forecast to reach $17.5 billion in 2005, a healthy 10% rise on the previous year. Overall, reckons a report from SAMBA, the kingdom's second-largest bank, about half of last year's growth in real GDP of 6.5% is attributable to the non-oil sector.

Buy the lot

Sound government policies have helped. In the past ten years the kingdom has issued over 40 new laws to streamline commerce, scrapping nearly all the onerous rules that used to insulate its economy. Well-regarded regulatory bodies now govern capital markets, telecoms and industrial standards. The country's patent office, which until recently had a ludicrous 50-year backlog of applications, has been radically reformed. SAGIA, the government's highly competent business-promotion arm, has ambitious plans to attract foreign investment. It should have an easy job. Foreign firms, recently granted the right to own land and hold majority stakes in most sectors, are now taxed at a modest 20% of profits and face no capital controls. Customs duties average just 5%, and are zero in trade with neighbouring Gulf states. The time it takes to license a business has fallen from six months to a couple of weeks.

Many of these reforms were part of the kingdom's effort to join the World Trade Organisation, in which it has now succeeded. More surprisingly, the World Bank last year ranked Saudi Arabia as the best place in the region to do business. But perhaps that is not so odd. The cost of living is far lower than in other Gulf countries, as are shipping, warehousing and licence fees. And the large Saudi market, with 23m people now and a forecast 33m by 2020, offers better prospects.

That population growth will require a huge investment in infrastructure. The hydrocarbon sector alone is expected to absorb some $100 billion in the next five years, says SAGIA's director for energy, Abdulwahab Saadoun. Meeting an expected doubling of electricity demand by 2020 will cost $150 billion. Similarly vast sums are forecast for roads, railways, airports and the water-desalination network that already supplies 60% of the kingdom's voracious demand.

Observers believe that this round of heavy spending will be far more judicious than that during the last great leap forward, in the 1970s. The era of paying lavish commissions on public-works contracts is over. Much of the new investment is in the form of build-operate-transfer contracts with private firms. Subsidies persist here and there: the price of household drinking water, for instance, is only one-seventh of the cost of distilling and piping it. But utilities and other state services are increasingly run on commercial lines. The role of the government is evolving towards that of a regulator rather than a provider.

All this bodes well, but the kingdom's recent success carries its own dangers. With a lack of other outlets for investment, share prices have risen to a giddy 40 times earnings. Some 3m Saudis, close to half the adult male population, now hold local equities. Sober financial minds fear that if the bubble were to burst, the middle classes would get hit. That, in turn, could start a backlash against the government's liberalisation policies, says Beshr Bakheet, a respected investment adviser.

A piece of the action

There is a simple way out. “It's a no-brainer,” says Prince Waleed bin Talal, whose own colossal Saudi portfolio has quadrupled in value since 2000. “The government should get out of all investment in public companies.” At the moment, it holds 55% of the stockmarket by value, including 70% of SABIC, 70% of STC, the local telecoms giant, and 69% of the National Commercial Bank, the country's largest. Prudent divestment of such assets would soak up

excess liquidity and quickly wipe out the state's $180 billion debt.

Yet despite the government's declared intention to press ahead, privatisation has lagged. That is a pity, and not just because of the danger of an overheated equity market. “There used to be growing income polarisation, but lately everyone has gained,” says Abdul Aziz Qasim, a clever Riyadh lawyer who, like many former Islamist radicals, has mellowed towards liberalism. “This has helped keep things quiet and returned legitimacy to the monarchy.” Mr Bakheet concurs. “Marx was wrong,” he says. “Money, not religion, is the opiate of the masses.” It may be no coincidence that the unrest in the 1990s coincided with a prolonged economic slump.

Mr Qasim suggests that the kingdom's best chance for future stability lies with shifting assets from the state to the public to change the underlying imbalance of power. As stakeholders rather than dependents, ordinary Saudis would be wary of taking risks, but would also be better placed to bargain for a stronger political voice. He is optimistic about progress on social issues: “If we can stick to the same pace of change for three years, there will be no going back.”

Saudi Arabia is not going to turn into Dubai. Subtract the bars and bathing beauties, however, and the holy cities, Mecca and Medina, are starting to look surprisingly like the boomtowns on the Gulf. It is not always a pretty sight. Rampant development combined with Wahhabist disdain for “idol-worship” has stripped away nearly all that is old. Time-share deals in both cities on anything from studio units to “royal suites” promise “visa facilitation” as part of the package. A wall of 20-storey brand-name hotels surrounds the shrine at Medina, which itself looks rather like a giant Arabian-themed shopping mall.

In Mecca, the 18th-century Fort of Ajyad, built as a defence against Wahhabist marauders, has been demolished. Rising in its place are seven apartment towers, six huge hotels and a four-storey shopping centre. Facing the main gate of the Great Mosque, the construction group Saudi Binladin (owned by the family of Osama bin Laden) is building a mammoth complex of skyscrapers for the Al Saud family. The tallest, at a height of 485 metres, will dwarf the great mosque's minarets. Mecca's Most Prestigious Retail Address, reads a billboard. No doubt it will still be there when the oil runs out.

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The US government's Energy Information Agency's Saudi Arabia Country Analysis Brief provides a good oversight of the Saudi economy, focused on the energy sector.

The Economic Reports series by Brad Bourland, Chief Economist at SAMBA, the Kingdom's second largest bank, are an indispensable resource: "The Saudi Economy: 2004 Performance, 2005 Forecast", "The Saudi Economy at Mid-year 2005", "Saudi Arabia: Third Quarter 2005 Economic Update".

Recent Books

"Saudi Arabia in the Balance", edited by Paul Aarts and Gerd Nonneman, Hurst and Company, London 2005. A sound collection of academic articles on Saudi politics and society.

"A History of Saudi Arabia", by Madawi al-Rasheed, Cambridge University Press, 2003. A competent brief history.

"The Complete Idiot's Guide to Understanding Saudi Arabia", by Colin Wells, Alpha Books, 2004. Excellent brief introduction, not just for idiots.

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Mobile TV

A fuzzy picture

Jan 5th 2006
From The Economist print edition

Mobile TV is coming—but how the market will develop is still unclear

Getty Images

Get article background

“THIS is a really exciting time—a new era is starting,” says Peter Bazalgette, the chief creative officer of Endemol, the television company behind “Big Brother” and other popular shows. He is referring to the upsurge of interest in mobile television, a nascent industry at the intersection of telecoms and media which offers new opportunities to device-makers, content producers and mobile-network operators. And he is far from alone in his enthusiasm.

Already, many mobile operators offer a selection of television channels or individual shows, which are “streamed” across their third-generation (3G) networks. In South Korea, television is also sent to mobile phones via satellite and terrestrial broadcast networks, which is far more efficient than sending video across mobile networks; similar broadcasts will begin in Japan in April. In Europe, the Italian arm of 3, a mobile operator, recently acquired Canale 7, a television channel, with a view to launching mobile-TV broadcasts in Italy in the second half of 2006. Similar mobile-TV networks will also be built in Finland and America, and are being tested in many other countries.

Meanwhile, Apple Computer, which launched a video-capable version of its iPod portable music-player in October, is striking deals with television networks to expand the range of shows that can be purchased for viewing on the device, including “Lost”, “Desperate Housewives” and “Law & Order”. TiVo, maker of the pioneering personal video recorder (PVR), says it plans to enable subscribers to download recorded shows on to iPods and other portable devices for viewing on the move. And mobile TV was one of the big trends at the world's largest technology fair, the Consumer Electronics Show, which took place in Las Vegas this week.

Despite all this activity, however, the prospects for mobile TV are unclear. For a start, nobody really knows if consumers will pay for it, though surveys suggest they like the idea. Informa, a consultancy, says there will be 125m mobile-TV users by 2010. But many other mobile technologies inspired high hopes and then failed to live up to expectations. And even if people do want TV on the move, there is further uncertainty in three areas: technology, business models and the content itself.

Tuning in

At the moment, mobile TV is mostly streamed over 3G networks. But sending an individual data stream to each viewer is inefficient and will be unsustainable in the long run if mobile TV takes off. So the general consensus is that 3G streaming is a prelude to the construction of dedicated mobile-TV broadcast networks, which transmit digital TV signals on entirely different frequencies to those used for voice and data. There are three main standards: DVB-H, favoured in Europe; DMB, which has been adopted in South Korea and Japan; and MediaFLO, which is being rolled out in America. Watching TV using any of these technologies requires a TV-capable handset, of course. Although several new models were unveiled in Las Vegas this week, no such handsets are yet available in Europe or America, and few in Asia.

In contrast, watching downloaded TV programmes on an iPod or other portable video player is already possible today. And unlike a programme streamed over 3G or broadcast via a dedicated mobile-TV network, shows stored on an iPod can be watched on an underground train or in regions with patchy network coverage. That suggests that some shows (such as drama) better suit the download model, while others (such as live news, sports or reality shows) are better suited to real-time transmission, notes Michelle de Lussanet of Forrester, a consultancy. The two approaches will probably co-exist. Future iPods may be able to receive real-time broadcasts, while mobile handsets will be able to store broadcast content or download it from PCs or PVRs for later viewing.

Just as there are several competing mobile-TV technologies, there are also many possible business models. Mobile operators might choose to build their own mobile-TV broadcast networks; or they could form a consortium and build a shared network; or existing broadcasters could build such networks. Some channels will be given away for free, while others are for paying subscribers only. The outcome will vary from country to country, depending on the regulatory environment and the availability of spectrum. In Italy, 3 bought Canale 7 to get its hands on its spectrum and its broadcaster's licence; in Britain, Finland and America, the scarcity of spectrum makes shared networks most likely.

The big question is whether the broadcasters and mobile operators can agree how to divide the spoils, assuming there are any. Broadcasters own the content, but mobile operators generally control the handsets, and they do not always see eye to eye. In South Korea, a consortium of broadcasters launched a free-to-air DMB network last month, but the country's mobile operators were reluctant to provide their users with handsets able to receive the broadcasts, since they were unwilling to undermine the prospects for their own subscription-based mobile-TV services.

Then there is the question of who will fund the production of mobile-TV content: broadcasters, operators or advertisers? Again, the answer is probably “all of the above”. Endemol's new mobile-TV division is talking to both operators and broadcasters about the commissioning of new shows, says Mr Bazalgette. But operators are newcomers to the world of television. Existing broadcasters have the advantage that they can use traditional TV to promote mobile content. But for operators, building mobile-only TV franchises will not be easy. Another problem is that mobile operators have yet to work out how to deal with advertisers. When Anheuser-Busch, a big drinks company, approached British operators about placing mobile-TV advertising, says Ms de Lussanet, it was passed back and forth between their technical and marketing departments.

Assuming the technology and the business models can be sorted out, there is still the tricky matter of content. At the moment most mobile-TV content is simply re-broadcasts of traditional channels, though in some cases programmes have been re-edited for mobile transmission. But the medium opens up many new possibilities, such as live streaming of raw material (as Endemol has successfully done with “Big Brother”), mobile-only “behind the scenes” content that complements traditional broadcasts, and entirely new, short-form programmes designed specifically for mobile transmission.

Since mobile phones are two-way, interactive devices, other possibilities include quiz shows in which the viewers are also the contestants, and programmes based on “viewer-generated” content. 3, for example, has a popular service called “See Me TV” which allows subscribers to upload short video clips. The author of the clip receives a small payment (1p in Britain, for example) each time the clip is viewed.

The potential for mobile TV is vast, in short—but so is the degree of uncertainty over how it should actually be put into practice. Most observers do not expect widespread adoption of mobile TV, if it comes at all, until 2008 at the earliest, since building the required ecosystem of technology, partnerships and content will take some time. Stay tuned.

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Corporate entertainment

Boy racers

Jan 5th 2006 | HONG KONG
From The Economist print edition

A cure for road rage and drink-driving

FOR many people, driving is bedevilled by traffic, potholes and parking problems. Hong Kong's wealthy motorists certainly get scant pleasure from their powerful Audis and Ferraris, given the city's hills, winding lanes and endless roadworks. But now the city also harbours an antidote. Nestled among the skyscrapers is the Sideways Driving Club, the world's first virtual racing centre, where speeds of more than 300kph are not only possible, but required.

The club's 12 Australian-made simulators are designed as training tools for real racing car drivers. With a narrow fibreglass cockpit, realistic steering system and a calibrated brake pedal, they mimic the feel of a genuine car, while a video screen shows the track and headphones provide realistic sound. The simulators can be programmed to drive like Formula One, Porsche Carrera, Le Mans or rally cars and drivers can choose from 250 courses, including all of the world's Grand Prix tracks. Customised software means all 12 cars are networked, allowing people to race each other and to add features such as pit stops and even the impact of worn tyres and fuel loads. Proof that this is not merely a souped-up arcade game lies in the fact that professionals are coming to Sideways to train, including Darryl O'Young, who won the Grand Prix in Macau last November.

With Shanghai now hosting a Formula One race each season, Carsten Widderich, a Hong Kong businessman and racing fanatic, decided to tap into the growing regional popularity of motor sport. As a former professional motorbike racer in his native Germany, Mr Widderich knew that many drivers, mechanics and enthusiasts owned a simulator or two for private use. Nobody, however, had thought to turn this into a proper business aimed at the corporate entertainment market—and this led to the birth of Sideways in December 2004.

Around two-thirds of the club's turnover comes from banks, brokers and companies. Events typically include up to three hours of driving; they also serve as a workout, since club drivers—just like real racers—typically lose a litre of sweat per hour. The club houses a bar, so drinking and driving is legal, though most customers quickly become too competitive to risk getting sozzled. Mr Widderich does not advertise, but says word of mouth has led to such interest that the club has repaid its $300,000 start-up costs in its first year.

The next step is to franchise the concept internationally. Sideways already has a partner to open a club in London's financial district this year and is planning sites in Shanghai, Beijing, Singapore, Seoul, Taipei and Kuala Lumpur. As a tip to new drivers, Mr Widderich says in certain races, like snow rallies, the fastest way to get around corners is to slide into them sideways—hence the club's name. An interesting thought, but best not tried on the real roads.

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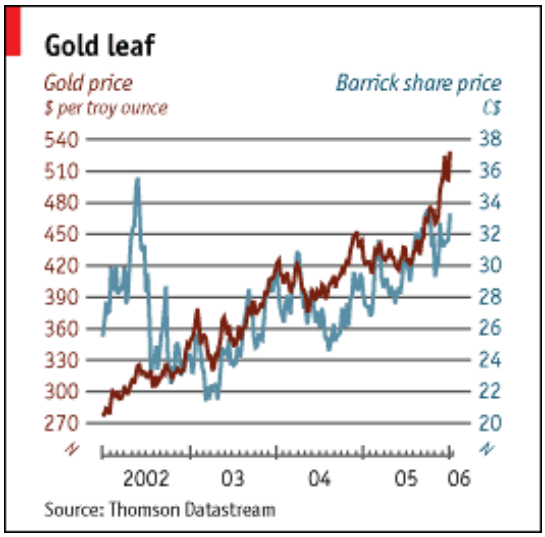
CLASSIC
PERTH 2006

The gold industry

Barrick's bet

Jan 5th 2006 | OTTAWA
From The Economist print edition

Rising prices fuel a merger boom



CREATING the world's largest gold company might normally be considered an acceptable reason to do a little bragging. The temptation is all the greater when the company in question, Barrick Gold, is Canadian and is wresting the crown from Newmont Mining, an American rival. Yet in describing Barrick's $10.4 billion friendly takeover of Placer Dome, another Canadian firm, Gregory Wilkins, the company's CEO, tied himself in verbal knots to avoid saying that the new entity—with a combined production of 8.4m ounces and reserves of 150m ounces—will be the new gold king. Perhaps he knows it will not last.

The deal is set to close on January 19th, but already analysts are speculating that Barrick's move will set off another round of consolidation, similar to one that started in 2001 when Barrick bought Homestake Mining, an American firm. In short order, Newmont acquired Franco-Nevada and Normandy Mining, Kinross Gold merged with Echo Bay and TVX Gold, and Anglogold, a South African mining giant, merged with Ashanti. David Cox of Metals Economics Group, a group of industry analysts, says the big gold companies are constantly chasing each other's tails, driven partly by the desire to be the top producer.

More than ego is involved. With the price of gold soaring well above $500 an ounce—touching levels last seen 24 years ago—gold-mining companies are scrambling to find new reserves. Exploration budgets were cut drastically in the late 1990s, when gold languished below $300 an ounce. New discoveries sank along with them. A brisk turnaround in exploration spending began in 2003, but the lag between initial discovery and confirmation of a find through extensive drilling means companies need speedier ways to replenish reserves. That means more acquisitions.

In choosing Placer Dome, Barrick had its eye on more than the 2.9m ounces it will add to production, and its 60.7m ounces of reserves. Both companies operate mines in Nevada, Australia and Tanzania, and Mr Wilkins estimates that the new entity could save at least $200m a year by combining everything from mining and processing to port clearance. That would help keep Barrick's production costs among the lowest in the industry, an advantage in the face of mounting pressures from high energy prices, a shortage of skilled workers, and appreciating currencies in Canada, Australia and South Africa.

Is bigger better for Barrick? Analysts answer with a qualified yes. Size brings diversity and the flexibility to manage risks. It makes the company's shares more appealing to big investors. But it also means that Barrick will hold the largest portfolio of fixed-price future sales in the industry, which will limit the extent to which it benefits from higher gold prices.

Reaching the top rung is vindication of sorts for Peter Munk, the founder and now chairman of Barrick. Mr Munk, who is less bashful about such things than today's managers, said ten years ago he wanted Barrick to become the world's largest gold-mining company. His plan almost derailed when Barrick made a tentative deal to buy Bre-X Minerals, a Canadian start-up in Indonesia. Luckily the deal fell through before Bre-X was exposed as a multi-billion dollar fraud. Just as well that Placer Dome has a long history behind it.

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CLASSIC
PERTH 2006

The Packer empire

The great inheritor

Jan 5th 2006 | SYDNEY
From The Economist print edition

Kerry Packer is gone, so what will become of his business empire?

BARELY two weeks before the death of Kerry Packer, an Australian media mogul, James, his son and heir, appeared as a witness in a Sydney court case involving one of Australia's biggest corporate collapses. Packer the younger was explaining his role as a director of One.Tel, a telecoms company that failed spectacularly in 2001, losing Publishing and Broadcasting (PBL), the Packers' listed company, an investment of A$400m ($296m at today's prices). Reflecting on the Packer empire, James told the court: “It's not mine at the moment, but one day it will be mine.”

That day came sooner than he thought when Kerry Packer finally succumbed to a gruelling history of heart disease and died, aged 68, on December 26th (see article). James, now 38, has taken over Australia's most powerful media empire. PBL owns Channel Nine, the country's biggest and most successful commercial television network, its biggest magazine stable, gambling casinos and pay-TV interests. All this is valued at about A$11 billion. Then there is Kerry Packer's personal fortune. He was Australia's richest man with assets worth an estimated A$7 billion, amassed through investments in media, property, ski resorts, cattle ranches and mining companies. Can the younger Packer possibly fill the shoes of a father who—even against Rupert Murdoch, his absentee competitor—bestrode Australia's corporate scene like no other figure in recent memory?

At first, the empire's future under James was overshadowed by his inauspicious involvement in the One.Tel affair. But he seems to have escaped any personal blame for the company's downfall. The received opinion, for the moment, is that Packer the younger is likely to have what it takes to make a success of the job. James had been groomed to take over eventually, ever since Kerry suffered a severe heart attack in 1990. In 1994 the Packer television and publishing empires were amalgamated into PBL, and James became executive chairman in 1998.

Largely at his initiative, PBL has expanded from its old media base into a series of profitable investments in casinos and new media, including Seek, a jobs website, and ninemsn, a search engine developed with Microsoft. Seven years ago, PBL bought Crown Casino in Melbourne, and it took over Burswood Casino in Perth in 2004. Strangely for a man who liked to gamble millions in the world's casinos himself, Kerry Packer opposed his son's Perth investment.

But the casino investments have turned out well: gaming is now PBL's biggest earner, accounting for 46% of the company's A$911m revenue in 2004-05. PBL has a joint-venture with Melco, an Asian gaming company, to open a casino in Macau in 2007. But in his first announcement since his father's death, James Packer said on January 3rd that PBL was pulling out of a proposal with Melco to build another casino in Singapore. His explanation—that “the expected returns are insufficient to justify the higher projected capital cost”—seemed to indicate that he was being more cautious in the wake of One.Tel.

Do Mr Packer's moves in new directions give weight to predictions from some quarters that he may be preparing to sell the Nine television network, his father's baby? The network has been struggling to keep its leading edge in ratings and advertising revenue. Three days before he died, Kerry Packer made a bid to rebuild ratings by offering A $780m for exclusive television rights for the Australian Football League (otherwise known as Aussie Rules). But the rights have gone to two rival networks. Even so, James Packer seems unlikely to sell the station.

Much will depend on plans by the Australian government to deregulate the media industry. This is likely to involve lifting curbs on foreign ownership, and on television proprietors owning newspapers in the same city. Kerry Packer was a formidable and successful lobbyist against any such changes, which would have opened his old media empire to competition. Now that he is out from under his father's shadow, James Packer is likely to look for ways to adapt that empire to the competitive world of new media.

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Ticket touting

Free-market fleecing

Jan 5th 2006 | AUSTIN AND SAN FRANCISCO
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The high price of fandom

Reuters

Texan triumph

THE last-minute victory of the Texas Longhorns in this year's Rose Bowl—America's college football championship—was the kind of thing that stays with fans forever. Just as well, because many had paid vast sums to see the game. Rose Bowl tickets officially sold for $175 each. On the internet, resellers were hawking them for as much as $3,000 a pop. “Nobody knows how to control [this],” observed Mitch Dorger, the tournament's chief executive.

Re-selling tickets for a profit, known less politely as scalping in America or touting in Britain, is booming. In America alone, the “secondary market” for tickets to sought-after events is worth over $10 billion, reckons Jeffrey Fluhr, the boss of StubHub, an online ticket market. Scalping used to be about burly men lurking outside stadiums with fistfuls of tickets. Cries of “Tickets here, tickets here” still ring out before kick-off. But the internet has created a larger and more efficient market. Some internet-based ticket agencies, such as tickco.com and dynamiteticketz.com act as traditional scalpers, buying up tickets and selling them on for a substantial mark-up. But others like StubHub have a new business model—bring together buyers and sellers, and then take a cut. For each transaction, StubHub takes a juicy 25%.

Despite its substantial commission—far higher than those charged by other online intermediaries including eBay or Craigslist—StubHub is flourishing. The firm was set up in 2000 and this year's Rose Bowl was its biggest event ever. The Super Bowl in early February will bring another nice haul, as have U2 and Rolling Stones concerts. Unlike eBay, which is the largest online trader in tickets, StubHub guarantees each transaction, so buyers need not worry about fraud. The company's revenues, now around $200m, are tripling annually (despite its start in the dotcom bust). And there is plenty more room to grow. Mr Fluhr notes that the market remains “highly fragmented”, with tiny operations still flourishing and newspaper classifieds not yet dead.

But there are risks. Some events are boosting prices to cut the resale margins; others are using special measures to crack down. This summer, tickets to the soccer World Cup in Germany will include the name and passport number of the original purchaser and embedded chips that match the buyer to the tickets.

Then there are legal worries. In America, more than a dozen states have anti-scalping laws of various kinds. New Mexico forbids the reselling of tickets for college games; Mississippi does so for all events on government-owned property. Such laws are often ignored, but can still bite. In Massachusetts, where reselling a ticket for more than $2 above face value is unlawful, one fan brought a lawsuit last autumn against 16 companies (including StubHub) over his pricey Red Sox tickets.

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Hilton hotels

Together again

Jan 5th 2006
From The Economist print edition

The two Hiltons re-marry

AP

We'll always have Paris

PARIS HILTON, an American socialite and heiress, makes a living out of exploiting a famous name. Her great grandfather, Conrad Hilton, built one of the world's best-known hotel chains. He also made some odd decisions, including cutting all of his children out of his will (which Paris's grandfather challenged successfully) and breaking up his company: in 1964 he sold its international division. But in an age when global brands are more important than ever, the two Hiltons are now finally being reunited.

Under the terms of the 1964 sale, Hilton Hotels, based in fashionable Beverly Hills, was responsible for the Hilton name only in North America. Everywhere else, the hotels have been run by the Hilton Group, a firm based in less fashionable Watford, just north of London. On December 29th Hilton Hotels announced it will buy the Hilton Group for £3.3 billion ($5.7 billion) from Ladbrokes, a firm of British bookmakers which has owned it since 1987.

The combined Hilton group will have nearly 2,800 hotels with 475,000 rooms in 80 countries, putting it head-to-head with global hotel groups such as InterContinental (owner of brands such as Holiday Inn and Crowne Plaza), Cendant (Ramada, Days Inn) and Marriott. Hilton's properties also include other brands, ranging from New York's upmarket Waldorf-Astoria to Conrad, Hampton Inn and Embassy Suites. With worldwide control of its brands, the company will try to expand abroad, especially through franchises.

Hotel operators are becoming more like brand-management companies. Indeed, the two Hiltons found it so important to forge a common marketing approach that in 1997 they began to share their reservation systems and reward programmes. Buying back its former international division was the “final and logical step,” says Stephen Bollenbach, chief executive of Hilton Hotels. The company will continue its strategy of selling hotels to investors whilst keeping agreements to run them, he added. The Californian company sold 20 hotels in 2005 for more than $1 billion.

Most of Hilton's expansion opportunities are outside America, especially in developing countries like China and India. In America the majority of hotel rooms are now operated by big brands, whereas in many other parts of the world hotels remain mostly independent. By offering franchises and management contracts, the large hotel groups provide owners with a steady flow of bookings from their global reservation systems.

The Hilton deal also opens up new opportunities for Ladbrokes. Mr Bollenbach is leaving its board, severing its American connection. This means Ladbrokes will feel free to expand its online gambling business—and take offshore bets from America, where online gambling is supposed to be illegal.

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Ford

Shrink to fit

Jan 5th 2006 | DETROIT AND LOS ANGELES
From The Economist print edition

Ford faces reality by getting smaller

EPA

Chill winds for Ford

ON JANUARY 23rd Ford is set to follow General Motors, announcing factory closures that will cut capacity to meet its fading share of the American market. Company insiders confirm it will lay out a plan to close a dozen assembly and parts plants, trimming up to 30,000 jobs. Most will be factory-floor jobs, but some 4,000 white-collar jobs will be eliminated—about 10% of the total—on top of 2,700 cut in 2005. Insiders suggest seven to 10 senior executives will be "encouraged to go away". Jim Padilla, the company's second-in-command and Stephen Lyons, the head of marketing, are expected to leave.

The plan (dubbed "Way Forward" in internal documents) has been drafted by Mark Fields, a 44-year-old assigned last autumn to run Ford's core "Americas" unit, by Bill Ford, the company heir and chief executive. Mr Fields, a graduate of Harvard Business School, was plucked from a job overseeing Ford of Europe and the Premier Automotive Group, two other struggling operations, after making his name turning round Ford's Mazda affiliate in Japan.

With his curly black hair and boyish grin, Mr Fields has often had to convince sceptics that he is a heavyweight. He will also have to deal with the cynicism that stems from the knowledge that he is the latest in a line of dynamic executives who have tried to turn around Ford. In the 1990s Sir Alex Trotman wanted to sculpt Ford into a global company, but his plans short-circuited. By centralising power in a few "corporate barons" in Detroit, he paralysed product development and undermined local marketing. The Trotman structure was demolished by his successor, Jac Nasser. The Nasser vision, with expensive forays into service and parts retailing, was modelled on Jack Welch's strategy at General Electric. But Mr Nasser's hectic style lost him the confidence of managers, dealers and, crucially, the Ford family.

So Mr Ford himself grabbed the helm over four years ago. His "back-to-basics" plan failed to anticipate rising competition from imports and the impact of soaring health-care costs. Add problems with Ford's European operations and recurring heavy losses at subsidiaries such as Jaguar, and Ford's automotive losses mounted to $1.7 billion through the first nine months of 2005: only its credit business will keep it in the black for all of 2005.

This month's headlines will be about closures and job cuts. But Mr Fields's real test will be fixing Ford's management. Part of his challenge will be to encourage risk-taking, not the sort of play-it-safe mindset that resulted in the big and boring Ford Five Hundred saloon, launched in 2004. It was supposed to help Ford regain its position on the passenger-car side of the business. But the full-size four-door car has not sold as well as expected, while a light 4X4 sport-utility "crossover" version has done so badly it will soon be pulled from the market. This mistake is all the more embarrassing because Chrysler, for years the weakest of Detroit's Big Three, has built its recent recovery in the market on a big, bold saloon, the Chrysler 300, a direct competitor to Ford's flop. Particularly troubling for Ford is watching things worsen in areas of traditional strength. Its Explorer sport-utility vehicle has seen sales slip from over 400,000 a year to barely 240,000.

All of this breeds frustration and confusion inside Ford. In a sense, says Dan Gorrell, of Strategic Visions, a Californian consultancy, that is good news: "They need to be scared enough to take action," he believes. At the same time, says one senior Ford official, "You've got to get people hopeful." Since arriving at headquarters, Mr Fields has tried to boost morale by making himself visible—eating in the cafeteria and holding regular internet video conferences. Ford does have some winners. Its huge F-Series pickups is setting all-time sales records. The stylish new Fusion sedan is also going down well.

Another element in Mr Fields's turnaround plan is to rethink the positioning of Ford's American brands. Traditionally, the Ford brand has played a “me-too” game, following the lead of General Motors. But today, in an increasingly fragmented market, it needs to have a clearer image. The strategy will be to develop brands that focus on younger buyers and on Ford's all-American identity. The company's lacklustre Mercury brand seems to be gearing its pitch toward women. And its luxury nameplate, Lincoln, is now little more than a market afterthought, surviving solely through limousine fleet purchases of its ancient Town Car. Its market has been colonised by Mercedes-Benz, BMW and Toyota's Lexus brand.

The sharp cuts to come suggest that Mr Fields and Mr Ford no longer envisage regaining ground lost in recent years, as market share slid from 25% to around 18%. Analysts, such as George Peterson, of AutoPacific, Inc., warn that the American market will soon resemble Europe's, with a handful of firms having roughly equal shares, rather than the traditional dominance of Detroit's Big Three. Speaking at the Los Angeles motor show on January 4th, Mr Fields acknowledged the new landscape since the emergence of Toyota, Honda and Nissan. “It looks more like a Big Six than a Big Three”, he said

Plant closures alone will not make Ford profitable in such an environment. Late last year, the United Auto Workers Union (UAW) grudgingly approved concessions on health-care costs, like those earlier granted to GM. But the narrow vote shows that workers remain sceptical about the severity of the current situation. The UAW contract, which runs through September 2007, limits Ford's ability to declare straightforward redundancies. Without the union's help, job cuts will largely be by natural attrition, boosted by some pay-offs. Otherwise, workers will go into a so-called “jobs bank”, drawing most of their pay and benefits for doing nothing.

That is the quintessential example of how difficult it will be for Ford (and its Detroit rivals) to make truly significant changes. Mr Fields desperately needs the flexibility to manage. If not, his restructuring plan could be just the latest in a string of failed strategies. Ford last year abandoned its aim, declared four years ago, of making a $7 billion profit by the end of 2006. Now the struggle is simply to make the car business profitable. This could be the last chance to fix Ford this side of the bankruptcy courts.

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Face value

Advertising's odd man out

Jan 5th 2006
From The Economist print edition

Landov

Maurice Lévy on the advantages of being French

THERE is something of the stage Frenchman about Maurice Lévy. From his stylish clothes to his impeccable manners and the relish with which he recounts the details of a particularly fine dinner, Mr Lévy plays the part. Unlike many other important French businessmen—who are pointedly indifferent about whether they are speaking in English or French—the chairman and chief executive of the Publicis advertising agency greets the news that the discussion is to begin in French by exclaiming "*Quel bonheur*" ("What joy"). When the conversation switches to English, his command of the language is immaculate—but his accent has none of the transatlantic twang of the younger generation of French executives.

The question of cultural identity is of more than personal interest. For Mr Lévy's company is the odd-man-out in the global advertising game. Four groups dominate the industry—Interpublic and Omnicom are based in America; WPP is a British company; only Publicis, the fourth largest, is based outside the English-speaking world. Mr Lévy's company has offices across the world and owns famous American and British ad agencies such as Leo Burnett and Saatchi & Saatchi. But his global empire is very firmly based on Paris's Champs Elysées.

Asked whether being based outside the English-speaking world is a disadvantage, Mr Lévy replies frankly—"Yes, in many ways." Marketing and advertising, he acknowledges, were "invented and developed by Americans", so Publicis has to approach the business with "humility". It also has a small home market—France accounts for just 3% of global advertising spending. For big potential clients in America or Britain, Mr Lévy acknowledges that "we may not be the obvious choice". Even the company's name can be a bit of a problem. Foreigners are not quite sure how to pronounce it. Mr Lévy toyed with the idea of changing the name. But in the end, he decided, "we are who we are". Being French would just have to be an advantage.

Mr Lévy argues that being outside the English-speaking mainstream has made the company much more alive to cultural differences. In the age of globalisation, Publicis has adopted the slogan "Viva la difference" and set itself firmly against the idea that companies should advertise with a single, global message. He argues that, on the contrary, effective advertising must be attuned to the way in which different cultures respond to different sorts of messages. For example,"The Americans are very direct; the British like to use humour; the French like something a little bit sexier. They will show a woman in the shower." At this point, Mr Lévy becomes briefly and uncharacteristically flustered; glancing across at the two women in the room, he remarks –"I'm sorry, but I am

French.” While many of his compatriots worry that the world is becoming more American, Mr Lévy thinks that when it comes to advertising, the Americans are becoming a little more European, and responding to messages that are emotional as much as rational. He cites a slogan crafted by the Publicis group for McDonald's—“I'm lovin' it.”

Like all the best ad-men, Mr Lévy spins a good story. But the prosaic reality is that the success of Publicis has more to do with a policy of bold and well-judged acquisitions than with any special French cultural sensitivity. Over the last decade the advertising industry has gone through a long period of consolidation which has seen famous names gobbled up: Young & Rubicam are now part of the WPP group; Abbott Mead Vickers were bought by Omnicom. Rather than being swallowed up itself, Publicis embarked on its own acquisition spree and has bought over 100 companies since the mid-1990s. The buying blitz is still going on. Last June, Publicis bought a majority-stake in Freud Communications, a fashionable London-based PR agency; and late last year it completed the acquisition of a 60% stake in Solutions Integrated Marketing, India's biggest direct-marketeer.

Bidding from the shadows

But Mr Lévy can also pull back from a deal. In September Publicis announced a takeover bid for Aegis, the last global independent buyer of ad space. The deal would have made Publicis the largest media-buyer in the world. But when a bidding war broke out and the price rose, Mr Lévy stepped away. The episode clearly rankles—and Publicis would probably jump back in for Aegis, if an opportunity arose. But Mr Lévy had made an important point: growth will not be bought at any price.

For the moment, the markets approve. Publicis's share price has risen by over 30% since April. The big ratings agencies have just awarded the company's debt an investment grade. And a recent report by Morgan Stanley predicts that the agency's revenues will grow faster than the industry average in 2006.

Such success might be expected to make Mr Lévy something of a hero in France, a country which is increasingly anxious about its economic future and about its ability to cope with globalisation. Yet he is treated with a certain suspicion. A recent profile of him in the left-leaning *Nouvel Observateur* called the boss of Publicis “an *éminence grise* with a shadowy network”. Perhaps so—but at least Mr Lévy's network was built through hard work, rather than social connections. Unlike much of France's corporate elite, Mr Lévy is neither the scion of one of France's big corporate families, nor a product of one of the country's elite graduate schools. He started in Publicis's computer department and worked his way up. In a country which has enshrined a 35-hour-week into law, he works famously long hours and has publicly castigated the French system for creating a “narrow and stunted” outlook in which “we paint ourselves as losers”. To the outsider, Mr Lévy may indeed come across as typically Gallic. But in his determined and successful embrace of global capitalism he is, unfortunately, out of tune with much of contemporary France.

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Energy security

Nervous energy

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From The Economist print edition

Corbis

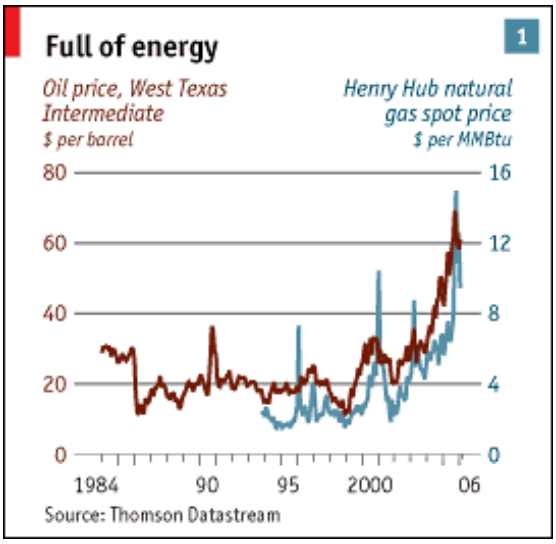
Consumers are highly vulnerable to a sudden break in energy supplies. But so are producers

IF YOU leave a loaded weapon lying around, it is bound to go off sooner or later. Snow-covered northern Europe heard the gunshot loud and clear when Russia cut supplies to Ukraine this week as part of a row about money and power, the two eternal battlegrounds of global energy. From central Europe right across to France on the Atlantic seaboard, gas supplies fell by more than one-third. For years Europeans had been telling themselves that a cold-war enemy which had supplied them without fail could still be depended on now it was an ally (of sorts). Suddenly, nobody was quite so sure.

Fearing the threat to its reputation as a supplier, Russia rapidly restored the gas and settled its differences with Ukraine. But it was an uncomfortable glimpse of the dangers for a continent that imports roughly half its gas and that Gérard Mestrallet, boss of Suez, a French water and power company, expects to be importing 80% of its gas by 2030—much of it from Russia. It was scarcely more welcome for America, which condemned Russia's tactics. And no wonder: it consumes one-quarter of the world's oil, but produces only 3% of the stuff. Over the coming years, the world's dependence on oil looks likely to concentrate on the Middle East, particularly Saudi Arabia. Russian oil had seemed a useful alternative.

Fear of the energy weapon has a long history. When producers had the upper hand in the oil embargo of 1973-74, Arab members of the Organisation of the Petroleum Exporting Countries (OPEC) cut supply, sowing turmoil and a global recession. When consumers had the upper hand in the early 1990s, the embargo cut the other way. After Saddam Hussein invaded Kuwait in 1990, the world shut in 5m barrels a day (b/d) of production from the two countries in an attempt to force him out.

With oil costing $60 a barrel, five times more than the nominal price in 1999, and spot prices for natural gas in some European and American markets at or near record levels (see chart 1), power has swung back to the producers for the first time since the early 1980s. Nobody knows how long today's tight markets will last. “It took us a long time to get there and it will take us a long time to get back,” says Robin West, chairman of PFC Energy in Washington. A clutch of alarmist books with titles such as “The Death of Oil” predict that so little oil is left in the ground that producers will always have pricing power. The question is how worried consumers should be. What are the threats to energy security and what should the world do about them? The answers suggest a need for planning and a certain amount of grim realism, but not for outright panic.



A classic tale

The unhappy history of Ukraine, Russia and gas is the story of energy security in miniature. When it comes to hydrocarbons, geopolitics and geology are inextricable. That is a problem for most countries in eastern Europe, which would love to get their energy from allies, and feel understandably twitchy about having their former master as a big supplier.

Russia sees it differently. It wants to use its energy riches to the maximum effect in the world market. It sees former communist satellite countries as nuisances, which scrounge subsidised gas, pay late if at all, and jeopardise sales to western Europe by brinkmanship about transit fees.

It is easy to understand why Ukraine and other Russian neighbours are exasperating Gazprom, Russia's huge gas monopoly. Its gas has long been siphoned off in vast quantities and Ukraine, like Georgia, has a dreadful record of falling behind with its payments. The main power station that supplies Moldova doesn't pay its bills at all. In 2005 Ukraine paid only $50 per 1,000 cubic metres of Russian gas, compared with the $240 paid by the EU. Now Gazprom says it wants to sell to these countries on a purely commercial basis.

That seems fair enough, but there is another dimension. Formally, at least, the $50 price is part of a framework that is supposed to last until 2009. Moreover, Gazprom is not asking for the same increase from each of Russia's neighbours. The independent Baltic states have two years to adjust. Georgia, which like Ukraine has an independent streak, faces a doubling of prices. Belarus, still friendly and dependable, is keeping its price and giving away part of the control of the pipeline to Russia instead. Gazprom and its chairman, Dmitry Medvedev, who moonlights as the head of Vladimir Putin's presidential administration, decided which deal is presented to which country. And Russia's way of pressing its case was an example of energy politics of the most brutal sort.

On January 1st, when Russia kept gas out of the “Brotherhood” pipeline crossing Ukraine, it also stopped gas from Turkmenistan and Kazakhstan, big suppliers to the country, from flowing through its pipes. Although enough was left for the rest of Europe, Ukraine simply tapped off some gas for itself as usual. “Theft”, Gazprom called it; though the Ukrainians asserted they were taking only the Turkmen and Kazakh gas that was due to them. For European consumers, the argument was academic. All that mattered was their shortages of gas: Italy experienced a fall of one-quarter; France, one-third; it was worse in countries such as Hungary, Austria and the Czech Republic, which get more of their supplies from Russia.

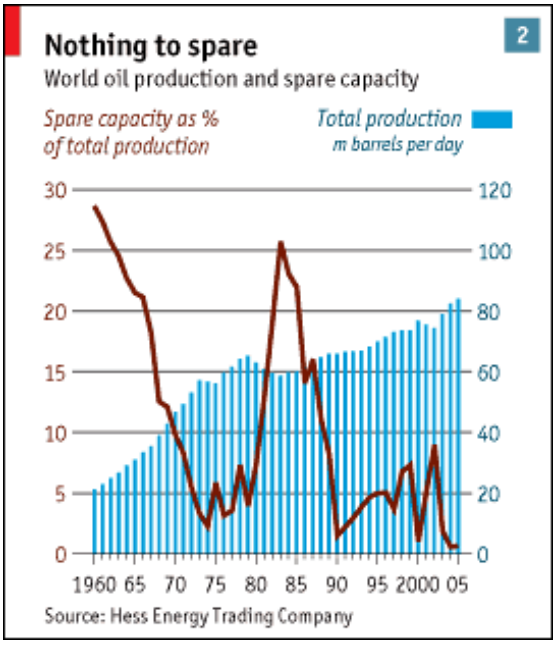
The tussle with Ukraine is only one of the fraught dealings Russia is having with its former satellites (see article). It even cut off the gas to Belarus two years ago. All such confrontations contain combustible mixes of the money, power and mishap that seem to bubble out of the ground whenever a huge supply of oil or gas is for sale. The risk of the whole business going terribly wrong is especially high when global markets have undergone a dramatic shift from glut to shortage, as they have in the past five years. Shifts disrupt the prices, power relations and patterns of consumption that everyone has learnt to live with. Suddenly everything is out of kilter.

Ever since the mid-1980s, when OPEC's attempts to keep the oil price high collapsed in the face of rising supply, only war has been potent enough to lift the price back to the levels of the 1970s. The difference today from the last era of high prices, says Tom Collina, of 20/20 Vision, an environmentalist group, is that “oil producers are pumping as fast as they can, but cannot keep pace with demand.”

The robust economic growth of America, coupled with industrial revolutions in China and India, has helped to ensure a very different market for energy. The world got used to relying on spare capacity of a few million b/d in

Saudi Arabia that could always cap price spikes in an emergency (it did just that in the first Gulf war and again during an oil-workers' strike in Venezuela in 2003). But demand has steadily eaten away reserves and investment has failed to keep up (see chart 2). In the tight markets for energy since 2004, some identified a “fear premium” of $10-15 a barrel reflecting the threat of lost supply. Even slower demand growth in 2005 did little to lower prices.

The tightness of capacity extends into refining and gas supply, leaving consumers vulnerable to any external shocks—such as the two hurricanes, Katrina and Rita, which hit the Gulf of Mexico in the autumn. The hurricanes put a dozen oil refineries accounting for 16% of US capacity temporarily out of action. American refining fell to its lowest level since March 1987, according to *Petroleum Economist*. The price of petrol rose above $3 a gallon—a level shockingly high to Americans, cheap as it might seem to Japanese or Europeans. Democrats accused the oil companies of price gouging, while Republicans argued for an easing of environmental laws restricting oil drilling and refinery building.



All this makes it a producers' world, which no one has exploited as gleefully as Hugo Chávez. Venezuela's president has always believed in oil as a tool of geopolitics, to be used against American “imperialism”. In 2004 he unilaterally raised the royalties on super-heavy crude production in the Orinoco belt from 1% to 16.6%—and may yet increase it to 30%. In 2005 he increased the tax rate paid by the foreign oil companies from 34% to 50%, and then hit them with huge bills for unpaid “back taxes”. The latest of his measures was to insist on the 22 foreign companies operating service contracts to switch, by December 31st 2005, to joint-ventures, in which the government would hold the lion's share. All but Exxon Mobil eventually did so.

At the same time, Mr Chávez has used cheap oil and refined products as “solidarity” to secure the loyalty of countries in the region. Those working against Mr Chávez have been threatened with a cut in supplies. Venezuela has bought almost $1.7 billion of Argentine bonds, helping Néstor Kirchner, its president, break free of the International Monetary Fund. This week Mr Chávez met the president-elect of Bolivia, Evo Morales, offering to supply the entire Bolivian diesel market in exchange for farm produce. “I don't want a cent for it,” he told Mr Morales at a press conference.

Strangely, perhaps, consumers can learn a comforting lesson from all this. For all his mischief-making, even a populist like Mr Chávez has never looked like cutting supplies to what Venezuela calls its “fundamental market” in America. Venezuela says it plans to sell some 350,000 b/d to China. But the Chinese market is ten times as distant, so much more costly to supply. America would notice a cut in Venezuelan supplies, which normally account for about 12-13% of its imports. But it could always buy oil on the world market (a better source than the illusory protection of drilling for oil in the Alaskan wilderness). Venezuela would be worse hit. It would be hard-pressed to find other markets for about half of its production, especially since most of its crude is high in sulphur and unsuitable for most refineries.

The futility of embargoes as a long-term strategy for energy suppliers is well understood in the Middle East, too, where bitter experience has taught that price stability is in everyone's interest. The Saudis, for instance, found that their market share dropped in the 12 years after the brief 1973-74 embargo during which they tried to keep prices high. They are only now making it up. Not only was the price rise unsustainable, but it also prompted reckless spending, led to social strains at home and drove consumers to protect themselves with oil taxes, conservation and a big expansion of oil production outside OPEC. Even Saddam Hussein in Iraq was always desperate for the cash from selling his country's oil. So, too, in Mr Putin's Russia. “Russia would be crazy to reduce its supplies to Europe,” says Paul Schapira, a specialist in European utilities at Goldman Sachs. “Europe depends on Russia as much as Russia depends on Europe.”

The long-term “energy security” risk, then, is less that of an energy tyrant holding the world to ransom, than that of unforeseeable short-term disasters or upheavals (which might, of course, involve tyrants). It is less of interrupted supplies than of highly volatile oil and gas prices, buffeted by hurricanes, workers' strikes and the chaos of an unpredictable world.

The biggest bogeys are terrorism and, in the Middle East, regime collapse, though in some ways the region is more stable now than it has been for a long time. Whereas only a decade ago there were half a dozen big territorial disputes, the prickliest today (outside Israel) is over a couple of islands between Iran and the United Arab Emirates and perhaps a brewing row between a future independent Kurdistan and a rump Iraq. Regime collapse may be overblown, too, since the first thing any new leader would want is cash from oil sales.

It takes a dedicated insurrection to destroy sprawling oil infrastructure. But there are danger points, such as the Saudi oil-shipment terminal at Ras Tanura, which handles some 4.5m b/d or Abqaiq, the world's largest oil-processing complex which treats something like 7m b/d. Were these to fall victim to a dirty bomb or some other devastating weapon, the damage to the world would be incalculable.

Gases to gases

Gas is arguably most vulnerable to unforeseen interruptions of supply. Oil is reasonably easy to trade, but in most gas markets the pipeline between the gas field and the gas burner locks producers and consumers in an exclusive embrace. But a market in tradable liquefied natural gas (LNG) is rapidly emerging—flows to Europe have more than doubled over the past decade and represent about one-quarter of the world's total cross-border gas trade. Some $100 billion could be invested in LNG over the next decade. This has big implications for the gas industry, because it is possible now to import gas from distant, underdeveloped producers at reasonable prices. Over the next decade, there might even be routine price arbitrage between markets.

Consumers have stocks and special reserves as insurance to be released amid the worst threats to energy supply. Perhaps, in what Mr West calls an “age of energy insecurity”, countries should ask if these provisions are enough. They can certainly also invest in energy conservation as a way of lessening the threat. But until the world weans itself off oil, there is no escaping the grim realism offered late last year to a congressional hearing by James Schlesinger, former secretary of defence: “We shall not end dependence on imported oil, nor...end dependence on the volatile Middle East, with all the political and economic consequences that flow from that reality,” he said. “Instead of energy security, we shall have to acknowledge and to live with various degrees of insecurity.”

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Pipeline politics

The energy empire

Jan 5th 2006
From The Economist print edition

Russia's energy riches are bringing it political power

GAS prices are only part of the game of energy politics Russia is playing with Europe. There is also a fierce contest about the merits of new oil and gas pipelines from east to west. Some of these would increase Russia's clout; others are planned to diminish it; pretty much all are contentious.

None more so than a proposed 1,200km, $5 billion pipeline along the Baltic seabed. To be completed in 2010, it will be 30% costlier than an overland version, but offers Russia's gas export monopoly, Gazprom, a direct link with its main west European markets. That will bypass Poland and the Baltic states, which had hoped for an alternative route bringing them extra transit fees.

Some doubt if it will ever be built. “I would just love to see a feasibility study of this project,” says one EU official. “They are just using it to put pressure on Poland and Ukraine to back down in transit negotiations,” he continues.

The new deal certainly threatens the Poles and Baltic states—and with more than lost fees. Russia could, at least in theory, cut off gas to them for political reasons, while continuing to supply western Europe. That has prompted fierce criticism—some politicians even call it the energy version of the Nazi-Soviet pact of 1939. Gazprom has recruited Gerhard Schröder, the former German chancellor, to the project. One Polish official terms it “a pact between the KGB and the Stasi”. The German boss of the pipeline, Matthias Warnig, is indeed a former East German spy. He worked with Vladimir Putin, now Russia's president, in St Petersburg in the 1990s.

The dilemma for Russia's gas customers, given the supplier's tarnished reputation for reliability, is whether to swallow hard and try to hook up to the new pipeline, or to diversify their sources of supply. For the northern post-communist countries, neither looks promising. Estonia and Latvia hope to join the new pipeline. Latvia has a huge and largely unused natural underground gas storage capacity. Its economy minister, Arturs Karins, says that this would be useful for western Europe too. But Wintershall, the German partner in the project, is dismissive.

That is bad news for the Baltic states, but hardly matters for Poland, which “does not want a single bucket more of Russian gas” according to one official. Poland's aim is to diversify its supplies as quickly as possible. Under a right-wing government Poland planned a pipeline to Norway. Though the next, ex-communist, administration cancelled it in 2002, this week's crisis might revive the idea along with other schemes, such as new nuclear power stations.

Perhaps more worrying for the ex-communist countries is Russia's investment in their domestic energy industries. Gazprom has been buying up distribution networks. Estonia, praised for selling equal stakes in its national gas company to Gazprom and a German investor in the 1990s, is now having second thoughts. Any attempt to diversify supply, for example by building a pipeline from Finland, could be stymied by the company that would need to buy, distribute and sell the gas.

In the end, small countries such as the Baltic states, or even a larger one like Poland, can do little on their own to ensure their energy security. The east European countries' hopes rest mainly on a common European energy policy. But that will need time, money and effort of a kind that the EU rarely devotes to immediate problems, let alone long-term ones.

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Japanese banks

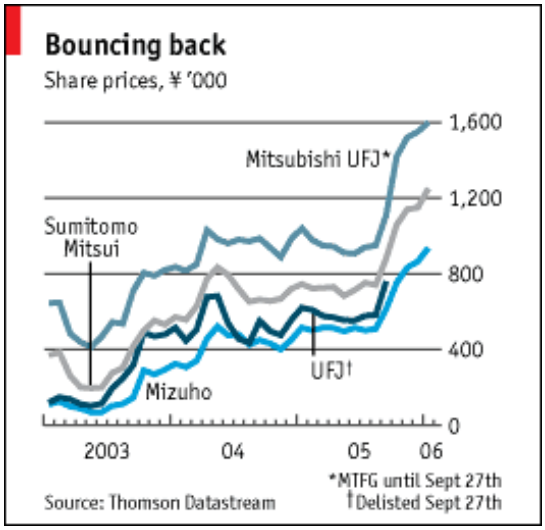
Open again for business

Jan 5th 2006 | TOKYO
From The Economist print edition

The question for Japan's megabanks is where new custom will come from

THE world's biggest bank, with $1.6 trillion of assets, opened for business on January 4th, and you are forgiven a few trips of the tongue before you can say “Bank of Tokyo-Mitsubishi UFJ” as readily as “Citigroup”, the number two. The new entity is the core bank of Mitsubishi UFJ, formed last autumn and one of three huge groups that now dominate retail banking in Japan. All are the products of mega-mergers. Mizuho, the second-biggest group, was formed in 2000 by crunching together Industrial Bank of Japan, Dai-Ichi Kangyo Bank and Fuji Bank; Sumitomo Mitsui grew in 2001 out of the merger of Sumitomo Bank and Sakura Bank. All these entities at the time were in the greatest distress, and deep concerns about the state of the financial system occasioned government intervention on a vast scale.

What a difference time, lashings of public money and strong-arming by regulators have made. At the peak, in 1986, Japan's top banks made up over a quarter of the Topix stockmarket index by capitalisation. At the nadir, in April 2003, when the sky still looked like falling, they accounted for just 2.7%. Since then, however, bank share prices have risen up to 16-fold (see chart); banks have been the engine driving Japan's stockmarket to five-year highs. Meanwhile, bad loans have been written off and losses turned to profit. Last autumn the banks announced record first-half profits. Mitsubishi UFJ alone expects full-year profits of ¥520 billion ($4.4 billion) in the year to the end of March.



Now banks are even thinking of expanding overseas for the first time since their sharp retreat in the Asian financial crisis of 1997-98. This week Bank of Tokyo-Mitsubishi UFJ was said to be thinking about investing $300m in the state-run Bank of China—which would be the first Chinese stake of any big Japanese bank. Many analysts and investors express a growing confidence that the megabanks have not only turned the corner, but have a sunny path before them. Are they right?

Certainly, the banks are far healthier than they have been in a long time. At the end of March 2002, the big banks' ratio of bad to total loans stood at 8.4%. The government subsequently gave them until March 2005 to cut the number by half. The banks beat that, bringing the ratio down to 2.9%, and by last September to 2.4%. At the same time, banks have rebuilt their capital. Today, capital-adequacy ratios stand at 11%, comfortably above the 8% required for international banks.

Of course, none of this would have been remotely possible without government help, which is now being repaid. Mizuho expects to repay its remaining ¥600 billion in public funds this year, and Mitsubishi UFJ and Sumitomo Mitsui expect to take a year or so longer to repay their remaining aid, ¥820 billion and ¥1.1 trillion respectively. Both profits and the ability to repay bail-out money have been greatly boosted by a recovering economy, which has allowed the banks to write back big amounts of bad-loan provisions.

There are lingering health concerns. One is over information-technology systems—the reason why this latest merger was put off by three months, so as not to have a repeat of glitches that plagued Mizuho. Another is the scale of non-recourse lending by banks to property funds. But by and large, says Toshihide Endo, director of the major-banks division at the supervisory bureau of the Financial Services Agency, banks have now “put their past problems behind them at last, and have managed to get to the point where they can build strategies for the future.”

And the strategies? Awkward question. Given that so much of the banks' recent profits comes from provisioning write-backs, profitability remains abysmally low by international standards. In the core business of lending to corporations, the market is still topsy-turvy: the weakest credits pay a lower rate of interest than stronger ones, partly because the maturity of such loans is shorter, but largely because to demand more would send many weak companies to the wall. Profitability from lending will presumably improve when the central bank finally abandons its policy of zero interest rates, perhaps next year. At that point, lending rates would rise faster than would deposit rates, and banks would pocket the spread.

But almost everybody expects companies to raise money more from debt markets in future, by-passing the banks. That is why the big three are looking increasingly at lending to small and medium-sized enterprises (SMEs) and to catering better to retail clients, a class wretchedly treated hitherto. Sumitomo Mitsui, in particular, is focusing on SMEs with less than ¥1 billion in annual sales. The bank no longer demands collateral, but runs sectoral portfolios of loans. It promises to respond to requests within three days, with loans of up to ¥50m. This type of lending has grown fast, much of it simply poached from smaller local banks. As for the longer-term potential of SMEs, Koyo Ozeki, credit analyst in Tokyo at PIMCO Japan, an international bond-fund manager, points out that such lending will not necessarily be an automatic answer for the banks, because of the pressure of competition on interest margins.

It's time to be nice

Hope is therefore fixed on retail banking, the former poor relation, to generate not just interest income but welcome fees. Drab branches are slowly being tarted up, renamed consulting centres. Some are even open at weekends. There has been some success selling new products: Sumitomo Mitsui, for example, has made a go of selling cast-iron dollar bonds, such as those issued by the World Bank, as well as bond and equity mutual funds. All three banking groups are big on mortgages, and are attracted by consumer finance.

Yet building solid retail businesses will prove hard. For a start, with Japan's population likely to fall (see article), demography is not on the side of the banks. Mortgage lending, certainly, has grown, but this reflects a one-off shift as people borrowing from public institutions remortgage with private ones. Meanwhile, deep cuts in branch networks over the past few years, welcomed at the time for bringing down costs, are now working against the sowing and harvesting of new revenues. David Atkinson, banking analyst at Goldman Sachs, calculates that, flat out, staff at Mizuho, which has the least appealing retail business of the big three, could spend at most 20 minutes a year with each of the bank's individual clients. That is an infeasibly short time to sell complex yet profitable financial products.

The big banks, in other words, while out of trouble, are now likely to be plagued by poor profitability and productivity. They will therefore face increasing pressure from investors to cut costs further, for instance, by streamlining or outsourcing cumbersome IT systems and by cutting staff. That could take years. Meanwhile, they will be tempted to seek profits abroad where they cannot be had at home. That may not be wise without a strong domestic base to build on; still, Citibank's snatching of Guangdong Development Bank (see article) must be galling for Japanese banks which have sat on the sidelines of the China game. One American banker puts it more bluntly. Will Japanese banks commit overseas some of the mistakes made in the past? “You bet.”

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Banking in China

A Chinese coup

Jan 5th 2006 | HONG KONG
From The Economist print edition

Citigroup pushes at the limits to foreign ownership in Chinese banks

IN A manoeuvre sure to incite the envy of its peers, Citigroup is poised to become the first foreign bank, and only the second foreign investor, to gain control of a Chinese lender. The American financial-services giant is leading a consortium that has bid some 24 billion yuan ($3 billion) for an 85% stake in Guangdong Development Bank (GDB), a medium-sized bank from China's relatively rich south. Citigroup itself could own 40-45% of GDB if the deal proceeds, making a mockery of rules limiting a single foreign investor in a Chinese bank to 20% and all foreigners to 25%.

This would be a comeback for Citigroup, which for two years has had to sit and watch while rivals have grabbed strategic positions in the Chinese banking market. In June 2005 Bank of America (BofA) beat Citigroup to a 9% stake in China Construction Bank (CCB), one of the country's four biggest lenders. Citigroup even lost a profitable position advising on CCB's multi-billion-dollar flotation. This time it has moved faster, outbidding ABN Amro, of the Netherlands, and France's Société Générale for GDB. Although Newbridge Capital, a private-equity firm, was the first foreign investor to gain management control of a Chinese bank, its charge, Shenzhen Development Bank, is barely half the size of GDB, which had assets of 345 billion yuan at the end of 2004.

Citigroup is, however, paying a high price: 2.3 times book value, compared with the 1.15 times BofA paid for its slice of CCB. True, acquirers often pay a premium for control. But GDB's financial state is precarious. Its liabilities exceed its assets by 35 billion yuan (state subsidies have propped it up); its capital-adequacy ratio is way below international standards; and its profitability is poor.

Moreover, to proceed with the deal Citigroup is being forced to restructure another, and at a price. In early 2003 the Americans bought 4.6% of Shanghai Pudong Development Bank, a middle-sized lender that insiders say is proving a prickly partner. Citigroup promised then not to invest in another mainland bank without Shanghai Pudong's permission. That has been granted, but only on condition that Citigroup raise its stake in the Shanghai bank to 19.9% at a rumoured cost of $800m, four times the original price per share. Remarkably, Citigroup also had to agree not to set up a joint-venture with GDB in credit cards, China's most promising financial business and the only one the Guangdong bank appears to be any good at.

Still, Citigroup's rivals will surely cry foul. By last October, 22 foreign banks had spent $16.5 billion on stakes in 17 mainland lenders, but had gained little real influence. The Chinese authorities will argue that GDB's poor state and smallish size make it an exception. And Liu Mingkang, the banking regulator, gave warning last month that should foreigners be granted more than a quarter of a Chinese bank, that bank would then be considered foreign, subject to restrictions that, among other things, allow yuan-denominated business in only a few cities. Still, he will now come under pressure to raise the caps on foreigners' stakes. That might allow the likes of HSBC, with 19.9% in BoCom, a larger and far sounder bank than GDB, to gain real management control. Inadvertently, Citigroup's coup may end up profiting its rivals more than itself.

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Currencies

A sinking feeling

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The dollar made a weak start to the year. Its slide could be unexpectedly steep

FOR Bill Gates, Warren Buffett and many Wall Street number-crunchers, the dollar supplied one of the nastiest surprises of 2005. The world's two richest men and most financial-market seers predicted that the greenback would fall last year, dragged down by America's colossal current-account deficit. Many forecasters were predicting that the euro would buy $1.40-odd by now and that a dollar would fetch less than ¥100.

They were all wrong. Although America's current-account deficit headed towards $800 billion in 2005, the dollar rose. It was up by 3.5% against a broad trade-weighted basket of currencies, the first rise in four years (see chart). Against the euro and yen, the greenback did even better. It ended the year at $1.18 per euro, up by 14%. Despite a wobble in December, the dollar made a similar advance against the yen.

Not surprisingly, the pundits are more cautious about 2006. Although most expect the greenback to end this year weaker than it began it, the typical forecast is that any decline will be fairly modest and take place mainly in the latter part of 2006.

That is because most analysts attribute the dollar's recent strength to widening differences between American, European and Japanese interest rates. These gaps are expected to grow for a few more months before closing slightly later in the year.

The Federal Reserve raised short-term interest rates eight times in 2005, to 4.25%. Japan, in contrast, kept the liquidity taps open and interest rates at zero, while the European Central Bank raised rates only once, in December, to 2.25%. Relatively higher American interest rates brought foreign capital pouring into dollar assets and pushed the currency up.

By this logic, as long as America raises rates faster than others, the dollar will stay strong. But as America's tightening campaign levels off and European or (maybe) Japanese rates rise, the dollar will weaken. The consensus, according to a recent compilation of forecasts by Reuters, suggests that the dollar could reach $1.25 per euro and ¥108 by the end of the year.

Judged by the first few days of 2006, those forecasts may prove too sanguine. The dollar suffered its biggest two-day drop against the euro in two years, and hit a two-month low of $1.21 against the European currency on January 4th.

One reason is that investors are becoming jittery about how soon the interest-rate gap might stop growing. The dollar swooned after the release this week of the minutes of the Fed's December meeting, which suggested that short-term interest rates might not need to go much higher.

An interest-rate gap that was merely stable ought to imply a weaker dollar. According to economic theory, it is the widening of interest-rate differentials that temporarily strengthens the exchange rate. Over time, an international difference in interest rates is offset by a drop in the currency with the higher interest rate.

Financial markets may also have become too obsessed with the influence of interest rates on currencies.

Historically interest-rate differentials have been little more use than anything else at predicting short-term movements in exchange rates.

And there are plenty of other reasons to worry about the dollar. One clear, albeit modest, source of support for the currency in 2005 was the one-off repatriation of American firms' foreign profits thanks to a one-year tax break. That is now over.

Oil exporters may prove more fickle dollar buyers than many expect. In 2005, as oil prices shot up, exporting countries saw their external surpluses soar. A good slice of these petrosurpluses found their way into dollar-denominated assets. That led some analysts to conclude that oil exporters were a safe and lasting source of dollar support. An alternative view is that the exporters, like others, were attracted by rising American interest rates. A recent study by the Bank for International Settlements, for instance, suggested that the currency composition of OPEC members' deposits has become more sensitive to interest-rate differentials.

China is yet another cause of uncertainty. Its eagerly awaited but ultimately minuscule exchange-rate shift in July 2005 was a boon for the dollar because it did not set in train a wider realignment of Asian currencies. This year the opposite may occur, with the Chinese allowing a bigger move in the yuan than markets expect. This week China introduced a system of marketmaking in spot yuan trading that could permit faster appreciation.

But the biggest shadow remains America's huge and rising current-account deficit. Reducing this will, at some point, require a much cheaper dollar. According to Jim O'Neill, of Goldman Sachs, fears over the current account lurked behind the scenes even in 2005. According to his models, interest-rate differentials alone suggest the dollar should be around $1.10 to the euro, or about 10% stronger than it is. He puts the discount down to nervousness about the current account. The real risk is that this nervousness takes centre stage just as the interest-rate gap fades. The result could be a sharp drop for the dollar.

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Deutsche Bank

A hard year ahead

Jan 5th 2006 | FRANKFURT
From The Economist print edition

Performing day by day, or even quarter by quarter, is not enough

EPA

Plenty for Ackermann to ponder

NORMALLY, a chief executive with such a record could laugh off calls for his resignation. He has led the company since its restructuring in 2002; it is producing record results; and there is no obvious successor. However, following an appeal court ruling last month calls for the head of Josef Ackermann, who runs Deutsche Bank, Germany's largest bank, are no joking matter. With five other men, he must face a retrial over his supervision of Mannesmann, a telecommunications company taken over by Britain's Vodafone nearly six years ago. Mr Ackermann plans to stay put. Officially he has the support of Deutsche Bank's supervisory board.

Mr Ackermann was on Mannesmann's supervisory board when it awarded bonuses and other benefits worth €57m (then $55m) to top officials in the wake of the company's €180 billion takeover by Vodafone in February 2000. Six Mannesmann officials, including Mr Ackermann, were tried over these payments. In July 2004 a Dusseldorf court acquitted them, though recognising a breach of German securities law. On December 21st, however, an appeal court in Karlsruhe, referring to the bonuses as “voluntary” gifts that brought the company no advantage, ruled that there should be a retrial.

That could tie up Mr Ackermann later this year with long hearings in Dusseldorf, as the first trial did in 2004. He remained at the helm then and will stick it out again, he says. Calls for his resignation from some newspapers and politicians have tended to ignore the presumption of innocence usually accorded those on trial.

But even without the new trial, this promises to be a testing year: Mr Ackermann, a usually mild-mannered Swiss, faces public opposition to his bank's strategy too, mainly from those in the press and politics who think it has neglected its home market. Though Deutsche Bank produced a record 27.6% pre-tax return on equity in the first nine months of 2005, the bulk of revenue came from selling and trading financial instruments. It has been trying to reduce this bias by beefing up its European retail operations: recently it agreed to share customers with ADAC, a motorists' club with 15m members.

But Mr Ackermann has been more concerned with increasing profitability than with broadening the footprint: he resisted political pressure to buy Postbank, the post office's banking arm, in 2004. Although Deutsche Bank has shown interest in expanding directly in neighbouring central Europe, it has favoured buying stakes in financial institutions in bigger markets farther afield, in Russia (United Financial Group), China (Hua Xia Bank) and Turkey

(Bender Securities).

Various strategic decisions in 2004 and 2005 suggest that the bank is still run principally from London as an investment bank rather than from Frankfurt as a broad wholesale and retail institution. That disappoints those in Germany who see Deutsche Bank as the only remaining candidate for a national champion to vie with the likes of UBS, HSBC and Citigroup. Specifically, Deutsche Bank cannot escape the perception that it is directed chiefly by its ten-strong executive committee, which sits in London and is dominated by investment bankers, and not by its four-man management board in Frankfurt. The supervisory board has power of control only over the management board.

So Mr Ackermann was pilloried last February for announcing job cuts in Germany within days of producing record results for 2004. The bank was criticised last month when DB Real Estate, a subsidiary, froze customer accounts in a property fund pending a revaluation of the buildings in the portfolio. This was unprecedented in Germany, but Deutsche Bank was surprised by the uproar it caused. It said hurriedly that it would consider compensating some investors. Still, quite a few have consulted lawyers. Unfortunately these events were linked with suspicions that the bank's asset managers, based in New York, had wanted to close the fund and sell the portfolio to private investors.

Having reached its profitability target, with the help of share buy-backs of more than €12 billion since 2002, Deutsche Bank needs to show that it can put on weight. Its market capitalisation is still only €45 billion, or $55 billion, a fraction of Citigroup's $245 billion and HSBC's $185 billion. Its biggest failing has been in institutional asset management, although it has Europe's second-biggest mutual-fund business. Deutsche Bank Asset Management has been losing institutional clients, particularly in London.

Mr Ackermann has done well for his shareholders: mainly by energising his investment bankers, he has produced the high quarterly returns that he promised. His task now, if he stays, is to show that Deutsche Bank can make lots of profit consistently. The best way of doing that may now be to win over its customers and its rank-and-file employees too.

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European insurance

Try anything once

Jan 5th 2006
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Broad expertise is the order of the day

INSURERS, bless them, don't have a reputation for being daring. That's the point, you might say: their job is to soften the impact of life's dramas. In fact, they are keener on novelty than you might suppose. Take architecture, of all things: Swiss Re's London office, known to locals as the Gherkin is just across the road from Lloyd's of London's inside-out colossus, still an eye-catcher 20 years after it went up. Increasingly, insurers are willing to change things in management, too. Several big European firms got new chief executives this week, and none of them are pure actuaries and underwriters, as the industry's bosses once were. Rather, they reflect the blurring lines between insurance and other financial disciplines.

Start with Swiss Re. When Jacques Aigrain took over from John Coomber as chief executive, the reinsurer's leadership passed from a man who started with the firm as an actuary 33 years ago —"an absolute classic of the old era," says a market observer—to a man who joined just five years ago, having spent two decades as an investment banker at J.P. Morgan with expertise in mergers and acquisitions. Nick Prettejohn, newly installed as head of Prudential's British unit, was in consulting and private equity before heading Lloyd's of London. Tim Breedon, the new boss at Legal & General, most recently ran his firm's £187 billion ($329 billion) investment arm.

"In the past, knowledge and experience in the insurance sector was always top of the list" for senior executives, says Simon Hearn of Russell Reynolds, a head-hunting firm. "That now comes halfway up the list." Analysts say the trend is more evident in Britain and Germany than in France, Spain or Italy. Turnover at the top has also accelerated in recent years.

Several factors account for the shift. Insurers, which make money from premiums and investing to offset claims payments, had a long run of poor underwriting years, which encouraged them to manage investments better. Although underwriting has since improved, they are still under pressure from shareholders to raise their financial returns. This is especially true of life companies, which need to match their assets to long-term liabilities.

Having developed the expertise to manage their own portfolios, some insurers (such as France's AXA and Britain's Aviva) have established asset-management arms to handle investments for clients. Others, including ING, of the Netherlands, and Allianz, of Germany, have gone further and offer banking too.

Insurers are also tied to financial markets in other ways. There is now a secondary market in tradeable products that can off-load risk to investors. Securitisation is growing. AXA, for instance, recently issued €200m ($242m) of asset-backed securities on its motor-insurance portfolio. Swiss Re last week securitised policies worth $370m, its second such transaction.

Underwriting, of course, remains a cornerstone. Analysts predict that premiums in Europe will rise in sectors affected by the big and costly hurricanes that battered America in 2005 (about half of the losses are likely to be borne by European companies). An added factor is the rising cost of reinsurance, which will be passed along to many primary insurers.

The chief executives taking office this week all lead profitable businesses. Others in the industry, though, face difficulties. Rating agencies have taken a harder line with insurers, especially since the big losses after the terrorist attacks in America in September 2001, issuing many more downgrades than in the past.

The slow growth of European markets, especially Britain, is another challenge. Big insurers are increasingly looking to developing markets for both customers and cost savings. Many have joint-ventures in India and China—although barriers to entry remain and few expect to make money soon. Martin Markus, a partner at McKinsey, says that

further cost savings could be achieved with cross-border co-ordination. Several firms are already servicing claims abroad. Aviva, for instance, now employs 6,500 people in India. It reckons it makes net cost savings of about 40% on activities there including telephone sales, claims management, data processing and invoicing. Mr Markus sees undertapped potential in cross-border underwriting too, including motor insurance.

A final factor is new regulations on capital levels, which favour insurers that are bigger and more diverse, since they generally experience less volatility and therefore a lower cost of capital. (European insurers, which tend to have both life and non-life businesses, are generally more diversified than American firms.)

The emphasis on size and diversity is likely to fuel further industry consolidation. Analysts say, however, that this is unlikely to be at the pace or on the scale of the last big wave, several years ago. They see greater potential for acquisition of medium-sized insurers within countries than big cross-border deals. This did not stop Mr Aigrain from helping to secure a recent deal to acquire part of General Electric's reinsurance business. It looks as if his M&A experience has already been useful.

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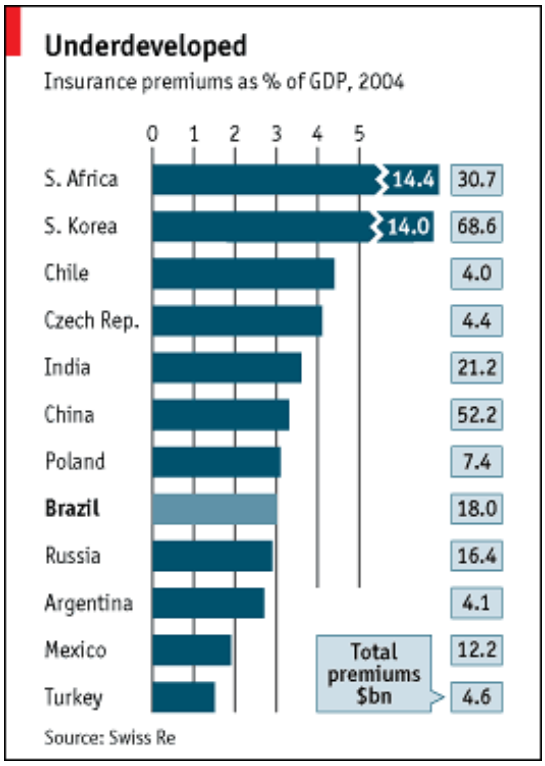
Reinsurance in Brazil

Opening up

Jan 5th 2006 | RIO DE JANEIRO
From The Economist print edition

Brazil's state-owned reinsurance monopolist prepares for competition



THE Brazilian Reinsurance Institute, now called IRB, must be one of the country's most hide-bound institutions. Founded 66 years ago by Getúlio Vargas, a Brazilian president who modelled much of his “new state” on Mussolini's, IRB has clung on to its monopoly through a military dictatorship, a return to democracy and an opening of financial markets. Brazil is the only big country where competition in ordinary insurance is free, but reinsurance—the assuming of part of the risk incurred by insurers—remains a state monopoly. Moreover, IRB is its own regulator.

Not for much longer. There are no plans to privatise IRB, but a bill in Brazil's Congress would open reinsurance to competition and take away IRB's regulatory powers. While Congress deliberates, Marcos Lisboa, IRB's energetic new boss, is driving it “as close to open market conditions as possible.” Foreign insurers, including Swiss Re and Munich Re, the world's top two, are expectant. About 13% of non-life insurance is reinsured in Brazil, compared with 19% in Argentina, 37% in Colombia and 50% in Chile. So there is room to grow in a market that in 2004 generated 45 billion *reais* ($15 billion) in insurance premiums. An added attraction is that Brazil is blessedly free from hurricanes and earthquakes, which have been plaguing reinsurers elsewhere.

IRB's monopoly has been a drag on the development of insurance for large, discrete risks, the sort for which reinsurance is most useful. Until recently it reinsured a standard menu of risks (it passes part of that on to the international market). Anything else has to be negotiated “one by one”, says João Pedro Paro of Tokio Marine, which recently bought an insurer in Brazil. This has held back everything from malpractice to export insurance.

Standard terms and pricing mean that good underwriters end up subsidising inferior competitors, says Beat Strebel, Swiss Re's chief in Latin America. Service is painfully slow. Unibanco AIG, one of Brazil's biggest insurers, waits up to 180 days for IRB to pay claims, says its boss, Luiz Eduardo Veloso. A tolerable delay would be one-third as long.

Mr Lisboa, an economist who as a senior finance ministry official helped write the law to end IRB's monopoly, took over at a low point in its history. Allegations that IRB funnelled money to political parties prompted the sacking of its top executives in June. Though highly profitable, IRB, which collected 2.4 billion *reais* in premiums in the first ten months of 2005, had been starved of investment. Mr Lisboa brought entrepreneurial zest, shifting the president's desk into an open-plan cockpit buzzing with the activity of the newly appointed directors. From here he pursues a strange dual vocation: stoking competition and preparing IRB for the consequences.

IRB now permits local insurers to seek quotes from foreign reinsurers; if it cannot better the price, the insurer can deal directly with the foreign group. This self-inflicted competition is already beginning to affect price and service. For good clients prices have dropped by 20-30%. The average time taken to settle claims has fallen from 400 days to around 100, says Mr Lisboa. “We don't exercise the power of monopoly” any longer.

Brazil's primary insurers are facing a difficult time. The industry pays out more in claims and for administration and sales than it collects in premiums, according to Fenaseg, the industry's federation. Insurers make up the difference

by investing in government bonds, on which real interest rates are among the world's highest. Now interest rates are starting to fall.

Although the opening of the reinsurance market should make life easier for some, it will increase the troubles of others. The end of the reinsurance monopoly will bring fresh capital, new products and tailor-made pricing, but mainly to insurers that already have in-house expertise, says Mr Veloso of Unibanco AIG. IRB will also become choosy, putting pressure on inefficient insurers that now depend on getting reinsurance cover on the same terms as everyone else. Mr Veloso expects that competition will spur takeovers of weaker players.

Might IRB itself become a casualty? Mr Lisboa has set up teams to develop new products and exploit IRB's data lode, plus an ombudsman charged with answering clients' questions within 24 hours. In December IRB increased a bulk property-insurance contract with foreign reinsurers and simultaneously cut its cost, prompting prospective competitors to grumble that the monopolist is still throwing its weight around. Mr Lisboa retorts that IRB is cutting costs and preparing for competition.

Chile's reinsurance monopoly shrank, but survived after liberalisation, Mr Lisboa notes. South Korea's still dominates its market. IRB may end up specialising, for example in dealing with smaller insurers that foreign giants overlook. The “main beneficiary”, Mr Lisboa acknowledges, should be the market as a whole.

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Economics focus

The long and the short of it

Jan 5th 2006
From The Economist print edition

America's bond market is upside down. Is the economy about to capsize as well?

SHORTLY before America's last recession, which began in March 2001, something odd happened to interest rates. Short-term rates rose above long. The same thing happened before the recessions of 1990, 1981, 1980, 1973, 1969 and 1960. A dark omen, then, but why worry about it now? In recent months, yields on short-term securities have crept up on those offered by longer-dated instruments. In the last week of December, it was (slightly) cheaper for the American government to borrow for ten years than for two.

This is unusual. The government borrows by selling a variety of IOUs, which promise to give the buyer his money back sooner (three-month bills, for example) or later (eg, ten-year Treasuries). Normally, the longer the maturity, the higher the yield a security must offer: the “yield curve” slopes upwards. Markets take this to be the natural state of affairs (though just why it should be so has taxed some of the best economists).

When things are upended, the yield curve is said to be “inverted”, a condition now exciting much chatter among analysts. Despite all this talk, the yield curve is not yet inverted across its full length. The yield on two-year Treasuries may have risen above that on ten-year bonds, but the rate on three-month bills still falls short by about 0.4 percentage points. The spread between ten-year and three-month securities has been this narrow twice before (in 1998 and 1995) without a recession ensuing. Nonetheless, the ironing-out of the yield curve is not normally welcome news. According to a statistical model estimated by Arturo Estrella*, an economist at the Federal Reserve Bank of New York, a spread of 0.4 points, averaged over a month, has historically signalled an 18% chance of recession within a year.

What gives the yield curve its predictive power? Long-term rates represent, in part, the market's expectations for future short-term rates. To see why, consider an investor who wants to lend for ten years. He could sink his money into a ten-year bond for the duration of its life. Alternatively, he could buy a five-year bond today, rolling his money over into another in five years' time. Suppose the five-year rate is 5% now, but the investor expects it to rise to 10% in five years' time. In that case, ten-year bonds must offer a yield of about 7.5% today to attract his money. On the other hand, if the investor expects five-year rates to fall to just 3% in five years' time, he will accept a ten-year yield of only about 4% today. In this case, long rates will fall below short now, in anticipation of even lower short rates later.

An inverted yield curve, then, suggests that short-term rates are higher today than they will be in the future. But why should this necessarily spell recession? Normally, it is because the Federal Reserve is in the midst of a campaign against inflation. To win this battle, short-term rates are sometimes raised high enough to induce a recession, which squeezes inflation out of the system. In due course, lower inflation will pave the way for lower short-term rates. But before this happens, long-term bond yields fall in anticipation of the future victory. In this case, an inverted yield curve is just a measure of the Fed's power.

Alternatively, inversions may be a measure of the Fed's ignorance. The bond market may know something the central bankers don't. Long-term rates may be subdued, because the market anticipates a recession that will eventually force the Fed to loosen monetary policy. But short-term rates remain high, because the Fed has yet to act on what the bond market foresees.

A portent and a puzzle

So does the flatness in today's yield curve mean that the Fed is trying to engineer a recession? Hardly. The Fed's rate-setting committee no longer describes its monetary stance as “accommodative”, but neither is it trying to cage a runaway economy. At 4.25%, its key rate is still much lower than the rate of growth in nominal GDP (more than 7%, annualised, in the third quarter), which serves as one crude measure of policy's tightness. According to the minutes of its December meeting, released this week, some members of the committee reckon that the federal funds rate is probably within a neutral range, one that should allow the economy to grow at close to its full potential.

In contrast to previous inversions, the yield curve is flat not because short rates are unusually high, but because long rates are unusually low. Yields on ten-year Treasuries have hovered around 4-4.5%, even as the Fed has hoisted short-term rates 13 times. Alan Greenspan, the Fed's chairman, himself does not fully understand why this is so—no doubt it has much to do with foreign purchases of long-dated American securities by oil producers and Asian central banks. Nonetheless, on this reading, the bond market offers a puzzling “conundrum”, as Mr Greenspan has put it, not a worrying omen. Optimists find comforting parallels in the events of 1966. In the last few months of that year, the interest rate on three-month bills edged above that on ten-year bonds, but no recession followed—the only time a fully inverted yield curve has cried wolf. Then, as now, long-term rates were unusually low, averaging under 5%.

The pessimists, however, look back five years, not 40. In the second half of 2000 the yield curve inverted, and then, as now, the vast majority of commentators dismissed it, arguing that the old portent had nothing to say about the new economy. Three months into 2001, the economy slipped into recession.

Although monetary policy may not be that tight as yet, the economy's strength may rely, more than most realise, on interest rates remaining low. To a disturbing degree, America's economy is still debt-led. Can this borrowing continue to drive growth now that interest rates are no longer “accommodative” and house prices are starting to cool? The answer is not easy to find in the bond market. But it will decide whether America's economy is as flat in the year ahead as the yield curve is today.

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* “The Yield Curve as a Leading Indicator: Frequently Asked Questions”. October 2005. Available at www.newyorkfed.org/research/capital_markets/ycfaq.pdf

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Clarification: National City Corporation

Jan 5th 2006
From The Economist print edition

National City Corporation of Cleveland, Ohio, asks us to make clear that it is not related to the National City Bank which was mentioned in "The very bottom line" in our issue of December 24th 2005.

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Psychology

Bayes rules

Jan 5th 2006
From The Economist print edition

A once-neglected statistical technique may help to explain how the mind works

SCIENCE, being a human activity, is not immune to fashion. For example, one of the first mathematicians to study the subject of probability theory was an English clergyman called Thomas Bayes, who was born in 1702 and died in 1761. His ideas about the prediction of future events from one or two examples were popular for a while, and have never been fundamentally challenged. But they were eventually overwhelmed by those of the “frequentist” school, which developed the methods based on sampling from a large population that now dominate the field and are used to predict things as diverse as the outcomes of elections and preferences for chocolate bars.

Recently, however, Bayes's ideas have made a comeback among computer scientists trying to design software with human-like intelligence. Bayesian reasoning now lies at the heart of leading internet search engines and automated “help wizards”. That has prompted some psychologists to ask if the human brain itself might be a Bayesian-reasoning machine. They suggest that the Bayesian capacity to draw strong inferences from sparse data could be crucial to the way the mind perceives the world, plans actions, comprehends and learns language, reasons from correlation to causation, and even understands the goals and beliefs of other minds.

These researchers have conducted laboratory experiments that convince them they are on the right track, but only recently have they begun to look at whether the brain copes with everyday judgments in the real world in a Bayesian manner. In research to be published later this year in *Psychological Science*, Thomas Griffiths of Brown University in Rhode Island and Joshua Tenenbaum of the Massachusetts Institute of Technology put the idea of a Bayesian brain to a quotidian test. They found that it passes with flying colours.

Prior assumptions

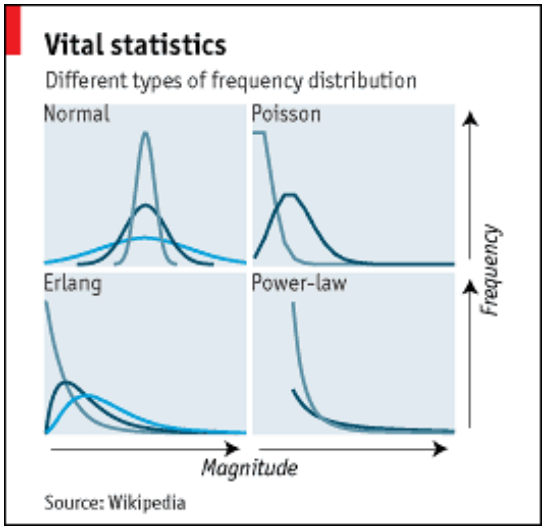
The key to successful Bayesian reasoning is not in having an extensive, unbiased sample, which is the eternal worry of frequentists, but rather in having an appropriate “prior”, as it is known to the cognoscenti. This prior is an assumption about the way the world works—in essence, a hypothesis about reality—that can be expressed as a mathematical probability distribution of the frequency with which events of a particular magnitude happen.

The best known of these probability distributions is the “normal”, or Gaussian distribution. This has a curve similar to the cross-section of a bell, with events of middling magnitude being common, and those of small and large magnitude rare, so it is sometimes known by a third name, the bell-curve distribution. But there are also the Poisson distribution, the Erlang distribution, the power-law distribution and many even weirder ones that are not the consequence of simple mathematical equations (or, at least, of equations that mathematicians regard as simple).

With the correct prior, even a single piece of data can be used to make meaningful Bayesian predictions. By contrast frequentists, though they deal with the same probability distributions as Bayesians, make fewer prior assumptions about the distribution that applies in any particular situation. Frequentism is thus a more robust approach, but one that is not well suited to making decisions on the basis of limited information—which is something that people have to do all the time.

Dr Griffiths and Dr Tenenbaum conducted their experiment by giving individual nuggets of information to each of the participants in their study (of which they had, in an ironically frequentist way of doing things, a total of 350), and asking them to draw a general conclusion. For example, many of the participants were told the amount of money that a film had supposedly earned since its release, and asked to estimate what its total “gross” would be, even though they were not told for how long it had been on release so far.

Besides the returns on films, the participants were asked about things as diverse as the number of lines in a poem (given how far into the poem a single line is), the time it takes to bake a cake (given how long it has already been in the oven), and the total length of the term that would be served by an American congressman (given how long he has already been in the House of Representatives). All of these things have well-established probability distributions, and all of them, together with three other items on the list—an individual's lifespan given his current age, the run-time of a film, and the amount of time spent on hold in a telephone queuing system—were predicted accurately by the participants from lone pieces of data.



There were only two exceptions, and both proved the general rule, though in different ways. Some 52% of people predicted that a marriage would last forever when told how long it had already lasted. As the authors report, “this accurately reflects the proportion of marriages that end in divorce”, so the participants had clearly got the right idea. But they had got the detail wrong. Even the best marriages do not last forever. Somebody dies. And “forever” is not a mathematically tractable quantity, so Dr Griffiths and Dr Tenenbaum abandoned their analysis of this set of data.

The other exception was a topic unlikely to be familiar to 21st-century Americans—the length of the reign of an Egyptian Pharaoh in the fourth millennium BC. People consistently overestimated this, but in an interesting way. The analysis showed that the prior they were applying was an Erlang distribution, which was the correct type. They just got the parameters wrong, presumably through ignorance of political and medical conditions in fourth-millennium BC Egypt. On congressmen's term-lengths, which also follow an Erlang distribution, they were spot on.

Indeed, one of the most impressive things Dr Griffiths and Dr Tenenbaum have shown is the range of distributions the mind can cope with. Besides Erlang, they tested people with examples of normal distributions, power-law distributions and, in the case of baking cakes, a complex and irregular distribution. They found that people could cope equally well with all of them, cakes included. Indeed, they are so confident of their method that they think it could be reversed in those cases where the shape of a distribution in the real world is still a matter of debate.

To prove the point, they actually did such a reversal in the case of telephone-queue waiting times. Traditionally, these have been assumed to follow a Poisson distribution, but some recent research suggests they actually follow a power law. Analysing the participants' responses suggests that a power law, indeed, it is.

How the priors are themselves constructed in the mind has yet to be investigated in detail. Obviously they are learned by experience, but the exact process is not properly understood. Indeed, some people suspect that the parsimony of Bayesian reasoning leads occasionally to it going spectacularly awry, with whatever process it is that forms the priors getting further and further off-track rather than converging on the correct distribution.

That might explain the emergence of superstitious behaviour, with an accidental correlation or two being misinterpreted by the brain as causal. A frequentist way of doing things would reduce the risk of that happening. But by the time the frequentist had enough data to draw a conclusion, he might already be dead.

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Scientific fraud

Egg on his face

Jan 5th 2006
From The Economist print edition

A leading stem-cell researcher is found guilty of fabricating his results

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AP

Game over

WELL, he made it up. All of it, apparently. According to a report published on December 29th by Seoul National University in South Korea, its erstwhile employee Hwang Woo-suk, who had tendered his resignation six days earlier, deliberately falsified his data in the paper on human embryonic stem cells that he and 24 colleagues published in *Science* in May 2005.

In particular, Dr Hwang claimed he had created 11 colonies of human embryonic stem cells genetically matched to specific patients. He had already admitted that nine of these were bogus, but had said that this was the result of an honest mistake, and that the other two were still the real McCoy. A panel of experts appointed by the university to investigate the matter, however, disagreed. They found that DNA fingerprint traces conducted on the stem-cell lines reported in the paper had been manipulated to make it seem as if all 11 lines were tailored to specific patients. In fact, none of them matched the volunteers with spinal-cord injuries and diabetes who had donated skin cells for the work. To obtain his promising "results", Dr Hwang had sent for testing two samples from each donor, rather than a sample from the donor and a sample of the cells into which the donor's DNA had supposedly been transplanted.

The panel also found that a second claim in the paper—that only 185 eggs were used to create the 11 stem-cell lines—was false. The investigators said the actual number of eggs used was far larger, in the thousands, although they were unable to determine an exact figure.

The reason this double fraud is such a blow is that human embryonic stem-cell research has great expectations. Stem cells, which have not yet been programmed to specialise and can thus, in principle, grow into any tissue or organ, could be used to treat illnesses ranging from diabetes to Parkinson's disease. They might even be able to fix spinal-cord injuries. And stem cells cloned from a patient would not be rejected as foreign by his immune system.

Dr Hwang's reputation, of course, is in tatters. The university is now investigating two other groundbreaking experiments he claims to have conducted—the creation of the world's first cloned human embryo and the extraction of stem cells from it, and the creation of the world's first cloned dog. He is also in trouble for breaching ethical guidelines by using eggs donated by members of his research team.

And it is even possible that the whole farce may have been for nothing. Cloned embryos might be the ideal source of stem cells intended to treat disease, but if it proves too difficult to create them, a rough-and-ready alternative may suffice. Another announcement made last month, by Andrew Bradley of Addenbrooke's hospital in Cambridge, England, estimated the number of human embryonic stem-cell lines that would be needed to create a reasonably functional therapeutic stem-cell bank in Britain.

These stem-cell lines would not give a precise genetic match, but they could be matched to patients in much the same way as is done with bone marrow and transplanted organs. The estimate, published in the *Lancet*, was that cell lines from as few as 150 donors could stock a "cell bank" suitable for treating most of the British population. Perhaps the therapeutic promise of embryonic stem cells need not rely on cloning after all.

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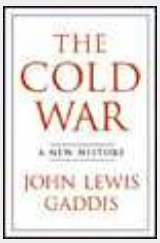
20th-century history

The blinking and the blinkered

Jan 5th 2006
From The Economist print edition

Russian archives, long closed to scholars, are adding crucial details to the old story of the cold war, as a new history shows

The Cold War: A New History
By John Lewis Gaddis



The Penguin Press; 400 pages; $27.95. Penguin/Allen Lane; £20

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Getty Images

WHERE does history end and current affairs begin? John Lewis Gaddis, who is often described as the dean of cold-war historians, has no doubts about his own special subject. To his students at Yale University, many of whom were still children when the confrontation with the Soviets ended in 1989, he writes, the cold war is “history: not all that different from the Peloponnesian War”. With a mixture of wistfulness and wonderment, Mr Gaddis notes: “When I talk about Stalin and Truman, even Reagan and Gorbachev, it could as easily be Napoleon, Caesar or Alexander the Great.”

It is partly in deference to a new generation that Mr Gaddis has decided to write a fresh and admirably concise

history of the cold war. With disarming frankness, he also admits that his agent had spotted a gap in the market. But Mr Gaddis's latest work avoids the obvious trap of simply being a summary of his earlier writings, the historian's equivalent of a “Greatest Hits” album. While the books that made Mr Gaddis's reputation, in particular his 1982 classic, “Strategies of Containment”, necessarily concentrated on the American perspective, his latest work provides a much more rounded picture by drawing on the flood of information that has come out from the Soviet side since the end of the cold war. Mr Gaddis recounts not only what Truman, Kennedy and Reagan were thinking, but also how Stalin, Khrushchev and Mikhail Gorbachev responded to the same events.

The reader learns, for example, how close the Americans came to winning the Korean war and creating a united, pro-western Korea. At one point Stalin seemed resigned to the defeat of North Korea. Mr Gaddis quotes him as “wearily” remarking: “So what. Let it be. Let the Americans be our neighbours.” The pro-western tide was turned only when Mao persuaded his own advisers that China must intervene, and sent 300,000 troops to support Kim Il Sung. Mao's baleful influence reappears in 1956. Khrushchev apparently agonised over whether to put down the Hungarian rebellion of that year, and his final decision to send in the troops was made partly “under pressure from Mao Zedong”. Spool forward to 1981 and Mr Gaddis provides a fascinating sketch of the Soviet leadership once again agonising over whether to crush the sprigs of political liberalism in eastern Europe. This time, they decided against sending troops to crush Poland's Solidarity movement, after receiving advice from their own top brass that, “The Polish armed forces are battle-ready and patriotic. They will not fire on their own people.” Soviet military intervention, warned the Kremlin's Mikhail Suslov, “will mean a catastrophe.”

The American side of the cold war has been familiar for a long time. But even here Mr Gaddis's mastery of the material, his fluent style and eye for the telling anecdote make his new work a pleasure. The reader comes across plain-speaking Harry Truman worrying privately about the need for a complete change in human nature if the nuclear age was not to be succeeded by the “insect age or an atmosphereless planet”. There is also the sleepless Richard Nixon leaving the White House in the early hours of the morning to argue with anti-Vietnam-war demonstrators gathered under the Lincoln Memorial. And there is the astonishment of George Shultz, a former economics professor turned secretary of state, when he discovers how eager his Soviet counterparts are to learn about the market economy. The didactic Mr Shultz even took to bringing pie charts to the Kremlin, to illustrate his arguments.

As is clear from Mr Shultz's career, the United States has an admirable habit of allowing the best minds in its universities to shape public policy. As one of America's leading historians, Mr Gaddis has been consulted by President George Bush on several occasions—notably just before Mr Bush made his second inaugural speech in which he pledged to “end tyranny” around the world. The admiration is mutual. Unusually for an Ivy League eminence, Mr Gaddis backed the Iraq war and praised the Bush administration for the boldness and vision of its foreign policy. And while he is too conscientious an historian to allow his political views to intrude upon his narrative of the cold war, a few minor passages hint at his real feelings: a trace of irritation in his account of General de Gaulle's anti-Americanism and an obvious admiration for the clarity and simplicity of the ideas of Ronald Reagan.

What lessons can be drawn from the cold war, now that it is safely consigned to history? Mr Gaddis's conclusions are warily optimistic. The cold war, he believes, introduced three new elements into global affairs. First, political leaders realised that some weapons were too dangerous to use; major wars fought between major states “had become...an anachronism”. Second, Orwell's vision in 1948 of the triumph of dictatorship proved blessedly wrong and so “the discrediting of dictatorships” was also a consequence of the cold war. Finally, “the globalisation of democracy” meant that the cold war ended in a “triumph of hope”. If those indeed are the lessons of the years of confrontation between the United States and the Soviet Union, then perhaps the cold war is not quite history yet. Its legacy lives on in the ideas of Mr Bush, and the men and women who advise him.

The Cold War: A New History.
By John Lewis Gaddis.
The Penguin Press; 400 pages; $27.95.
Penguin/Allen Lane; £20

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God and philosophy

Chicken soup for the brain

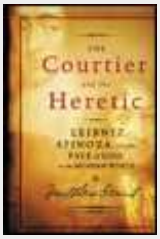
Jan 5th 2006
From The Economist print edition

GOTTFRIED LEIBNIZ and Baruch de Spinoza (known also by his Latin name, Benedictus, and to his friends as Bento) were among the giants of the 17th century. Ever since then, their ideas have exercised a huge influence over the way people think about almost everything. Both philosophers reflected a great deal about the existence of God, and believed in a kind of God; but they also played a part in the modern era's shift of consciousness from a God-centred view of reality to a man-centred one.

They grew up, of course, in the same historical context: a Europe that was exhausted by religious wars. Whether openly or secretly, many Europeans were yearning for a liberation from theocracy, if only for the sake of a quiet, prosperous life.

But as Matthew Stewart's absorbing study of the two philosophers shows, they were not merely born at different points on Europe's spectrum; they reacted to their circumstances in diametrically opposing ways. Spinoza's family were Iberian Jews who had found refuge in the relative tolerance of Amsterdam; Leibniz was born into the Christian establishment as the son of a philosophy professor in Leipzig. Both had an early experience of rejection: Leibniz had his doctorate turned down, while the young Spinoza's fate was even harsher. The Jews excommunicated him for heresy, partly for his refusal to accept the literal truth of the scriptures.

The Courtier and the Heretic: Leibniz, Spinoza, and the Fate of God in the Modern World
By Matthew Stewart



Norton; 320 pages; $25.95.
Yale University Press; £16.95

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Spinoza responded with the equanimity of a “secular saint”, as he is sometimes described. He learned to polish lenses as a way of making a living, and lived out the last 20 years of his life in a modest but dignified way, wrestling relentlessly with ultimate questions with little apparent fear of God or man. Leibniz, by contrast, was a political animal. He made himself useful to one worldly master after another, and was always conscious of the political consequences of ideas. Among his concerns was to demonstrate that the Protestant and Catholic faiths, as well as the secular reasoning he brought to logic and science, were all compatible with each other.

As a defender of religious orthodoxy, Leibniz felt obliged to attack Spinoza on many points where the latter seemed heretical: for example, Spinoza's rejection of the idea of a personal God, with “human qualities”, and his disbelief in personal immortality. What Mr Stewart shows is that Leibniz, despite himself, was fascinated by Spinoza's teachings and acknowledged their power.

The two men met just once—in The Hague—and Mr Stewart's reconstruction of the encounter (complete with evocations of the creaky floorboards, autumn winds and scent of chicken broth) forms the high point of his narrative. Their discussions extended over several days, and seven years later Leibniz described his host as a man “who says what he believes is true” and who believes (however erroneously) “that he is serving all humankind in delivering it from ill-founded superstitions.” It is not easy to write of intellectual ideas about God and the smell of soup on the same page, especially when the evidence for the incident being described is quite patchy. But Mr Stewart, a former management consultant with a doctorate in philosophy from Oxford University, manages pretty well.

In doing so, he lays the ground for a new genre: rigorous, readable intellectual history for the reader who would never buy a work of pure philosophy, but wants to know why people think the way they do. If accessible books about ideas are becoming increasingly popular, it is perhaps because many liberal-humanists (including the canal-dwelling Dutch bohemians who today inhabit Spinoza's old haunts) feel nonplussed by the muscular Christianity of the current American administration and a resurgent Islam that puts God at the centre of its world.

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Exploring west Africa

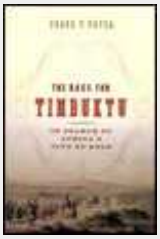
Desert storm

Jan 5th 2006
From The Economist print edition

POPULAR images of African exploration come mostly from the east of the continent, which was scoured by young buccaneers for the source of the Nile and where, in 1871, Henry Morton Stanley, an American, presumed to find Dr David Livingstone. Yet for a wave of explorers who braved Muslim fanatics and malarial mosquitoes almost a century before, west Africa was the great enthusiasm.

Timbuktu, which stood at the centre of this fantasy of discovery, had been imagined, and coveted, by Europeans for 500 years—ever since its ruler Mansa Musa visited Cairo on his way to Mecca in 1324 with a retinue of 60,000 men and 80 camel-loads of gold. But finding Timbuktu, at the confluence of Arab and black Africa, between the Sahara and the feverish coast, was a problem. Nor was nature the main obstacle: Arab and African leaders were often hostile. They knew enough about early 19th-century European expansionism to fear the white armies that were bound to follow in the explorers' footsteps.

The Race for Timbuktu: In Search of Africa's City of Gold
By Frank T. Kryza



Ecco; 352 pages; $25.95

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Just as its rulers were determined not to allow these European travellers to advance, so was west Africa's local citizenry often unhelpful and unimpressed. On entering Kano, now in northern Nigeria, Lieutenant Hugh Clapperton, an Englishman, found 12 miles of town-walls and 40,000 inhabitants. He wore his best Royal Naval rig for the occasion, but needn't have bothered: he reported that, “Not one individual turned his head to gaze at me, but all, intent on their own business, allowed me to pass by without notice or remark.” Major Alexander Gordon Laing, who in 1826 finally became the first European to enter Timbuktu, found to his dismay that the city's former glory was barely remembered. Where 25,000 Koranic scholars had once laboured in great libraries, only 12,000 dusty people remained.

Frank Kryza's is an engrossing and well-organised account of these places and the Europeans who explored them. Although his writing is scarred by the occasional dreadful sentence (“One would not have guessed, from his appearance, how bloodthirsty his uncle had been”), his book is well researched, and he paints a vivid portrait of the contradictory characters of the many rival explorers.

One was Mungo Park, a handsome Scottish doctor, who tried to slaughter his way down the River Niger much as Stanley would later down the Congo—and who got his just desserts in a mysterious death. Clapperton and his co-explorer, a lusty toff named Lieutenant Dixon Denham, hated each other to the point of communicating only by letter. Most engaging was Laing, who disguised himself as a Muslim, except on Sundays, when he would appear as an Englishman. He reached Timbuktu in a terrible state, with 24 gaping wounds, including a musket-ball through the back, a hacked wind-pipe, flayed scalp, broken arm and fingers, and with an ear sliced in two. Yet, he wrote home, “I am nevertheless doing well, and hope to return to England with much important geographical information.”

Laing was murdered shortly afterwards and his journals lost. The incident sparked a row, and almost a duel, between the British and French consuls in faraway Tripoli, hastening regime change there, and later colonisation. In such ways was the Great Powers' Africa policy made.

The Race for Timbuktu: In Search of Africa's City of Gold.
By Frank T. Kryza.
Ecco; 352 pages; $25.95

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Camille Claudel

The triumph of tragedy

Jan 5th 2006 | PARIS
From The Economist print edition

A sculptress who carved sensuality from stone

MUSE, model and modeller, Camille Claudel was above all an Impressionist in three dimensions. This much is evident from a small, jewel-like exhibition that opened recently in a 19th-century Paris mansion, home to an incomparable gallery of Monets. Claudel's work reflects and reverberates with light, and she shares with the painter from Giverny a particular ability to capture natural forms and atmospheric moments in art.

Claudel's gift was her innate talent for creating sensual sculptures that pulse with life and seem to defy gravity. Her tragedy was to break all the rules of bourgeois society. Octave Mirabeau, a French writer, was astonished at Claudel's artistic genius, a talent that women at the time were thought not to possess. When Mirabeau wrote that Claudel was a “revolt against nature”, he meant it as a compliment.

Claudel's childhood love of modelling was nourished in school and she made powerful portrait busts of her family while still an adolescent. When her father, a provincial bureaucrat, moved his children to Paris in 1881 to further their education, a family friend exclaimed: “You must have studied with Monsieur Rodin.”

Claudel had yet to meet France's most famous sculptor; only later would her fame rest on their liaison. Twenty-four years Claudel's senior, Auguste Rodin took her on as an assistant in 1884, turning her into his model and mistress by the time she was 20. Rodin was at first besotted with her, and vowed to take no other student. He introduced her to the Paris *beau monde* and she gained prominent patrons. Famously, he wrote: “I showed her where to find gold, but the gold was within her.”

Claudel, on the other hand, gave him her life and her youth. Working daily in his studio, she created many of the figures in Rodin's most famous works, including “The Gates of Hell” and “The Burghers of Calais”. Rodin's art was rejuvenated by their love affair, with intertwined erotic couples appearing in his art after their relationship began. Theirs was a union of art, mind and body; the affair is the centrepiece of another small show in Detroit. Rodin promised to marry her, but he never did. In 1898 they separated when he refused to leave his long-term mistress Rose Beuret, an older woman who managed his studio and cared for him in his old age.

From this point on, Claudel's life begins to read like a Russian novel. Wracked with depression, yet still proud of her talent, Claudel took her own studio. But many of her patrons deserted her when she broke with Rodin, and official commissions were scarce without his connections. She fell into debt; in 1913, her neighbours began to complain of a madwoman in the basement, and her mother had nurses sent from a local asylum to take her away.

Rodin, though, never lost sight of Claudel's importance as an artist. A year later, while he was creating his Paris museum, he reserved a space for work by Claudel, which can still be viewed there today. Claudel, however, never saw the final result. She remained locked up, despite doctors' reports that she had recovered, until her death in 1943. Terrified of never being set free, Claudel wrote to her brother, by then a poet of some renown: “The dream that was my life has become a nightmare.”

Claudel's letters are particularly moving when contrasted with her expressive sculptures that evoke both pain and joy. She refers to her exquisite Perseus holding the head of Medusa as “he who kills without looking”. As you look at this Greek hero who defeated madness with reason, gazing at his conquest only in a mirror (looking at her directly would have killed him), the gorgon's features seem to resemble those of their artist-creator.

Claudel's work fights against sculpture's static nature. Light flickers across her supple forms and enigmatic spaces open up between figures, forcing the viewer to examine her pieces from every angle. This is most apparent in the room devoted to eight different versions of her most famous work, “The Waltz”, among the most erotic pieces in

western art. A semi-naked couple is swept up in a whirlpool of music and passion, she swaying into his arms, while his arm encircles her, twirling them endlessly on in seemingly helpless fusion.

For more than 30 years Claudel's great niece, Reine-Marie Paris, has worked to retrieve the sculptress from oblivion, uncovering art and correspondence that was scattered across Europe. Most of the work in this show belongs to her. Claudel fits well into the Musée Marmottan's programme of exhibitions, which has been devoted to women artists of the 19th century, such as Mary Cassatt, Berthe Morisot, Eva Gonzalez. But this exhibition is a disappointment. The museum presents Claudel's work accompanied by a few photographs, a brief chronology of her life and a mawkish film, without investigating her talent as an artist or attempting to understand how and why she made each piece. Quotes from Rodin and her brother, Paul, are scattered about the show, but there is little of Claudel's writing on display, even though her correspondence has been published and is for sale in the bookshop. It seems unjust that Claudel should still be seen but not heard. After all these years, surely she deserves better.

“Camille Claudel” is at the Musée Marmottan Monet, Paris, until January 31st.

“Camille Claudel & Rodin: Fateful Encounters” is at the Detroit Institute of Arts until February 5th.

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New cinema

Like it was

Jan 5th 2006 | LOS ANGELES
From The Economist print edition

A romance to relish

THE first frames of Terrence Malick's “The New World” show tall ships sailing into a bay. The Powhatan tribesmen gather on the banks to marvel; water trickles through overhead bars on to the rapturous face of the captain, John Smith. Wagner's music swells as one glorious image succeeds another to match the words John Adams wrote in his diary: “I always consider the settlement of America with reverence and wonder.” Yet when the last chords have died away and the celluloid colonists venture into the tall grass for their first encounter with the “naturals”, you know that all the elements are in place for a tragedy.

The materials are familiar. Sent on a visit to the Powhatan emperor, Smith (Colin Farrell) is spared at the insistence of the emperor's favourite daughter, Pocahontas (newcomer Q'Orianka Kilcher, who was only 14 when the film was shot). This event, described in Smith's history of the Jamestown colony, probably never happened, but it is still one of the central myths of America's history.

There was a real Pocahontas, who helped Smith, married a Puritan gentleman, John Rolfe (Christian Bale), returned with him to England to be presented at court and died on the journey home. It is her story, fused with Smith's romantic yarn, that Mr Malick tells. The three protagonists' voices, like the lyrical musings of the soldiers fighting the battle of Guadalcanal in his previous film, “The Thin Red Line”, weave their counterpoint to a love story in the great Hollywood tradition: Smith's yearning for a paradise on earth, Pocahontas's lament after he has abandoned it and her, and Rolfe's hopeful kindness as he first claims and then loses her in turn.

Along the way lie many marvels: the sublime, outlandish images of the Emperor's palace recorded by Smith's pen, and the delightful portrayal of London as seen through the eyes of Pocahontas, who is as much an object of astonishment and delight to the English as they are to her. But the heart of this dreamlike film is the idyll that John Smith and Pocahontas enjoy in the wilderness. Fans of Mr Malick's earlier films—“Badlands” and “Days of Heaven”—which were coolly cerebral despite their visual splendours, will be surprised by the naked emotion of these passages, but they are the reason why “The New World” is this gifted director's most beautiful film.

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Amazon worldwide bestsellers

The big book index

Jan 5th 2006
From The Economist print edition

What Santa carried in his Christmas sack

FATHER CHRISTMAS is the man to ask if you want to know why the world is at, why you have eyebrows, why the best food comes from Italy, why drug dealers live with their mothers, or why for some people everything is shit. Which may be why more books are sold in December than in any other month.

1. The Chronicles of Narnia (Boxed Set).
By C.S.Lewis. HarperTrophy; $28.77. HarperCollins; £22.79

The release of the film of Narnia in time for Christmas provided just the right opportunity for a special re-issue of all seven of the C.S. Lewis books, although re-arranging them in chronological order has caused turmoil in the kingdom.

Click to buy from Amazon.com or Amazon.co.uk

2. Does Anything Eat Wasps?: And 101 Other Questions.
By New Scientist magazine. Profile Books; 256 pages; £3.76

Perfect if you want to know how long you can live on beer alone, why you have eyebrows, or whether a compass works in space.

Click to buy from Amazon.co.uk

3. The World is Flat: A Brief History of the Twenty-First Century.
By Thomas L. Friedman. Farrar, Straus and Giroux; 496 pages; $18.15. Penguin/Allen Lane; £14

The *New York Times* columnist and three-times Pulitzer prize winner explains how globalisation has made the world smaller.

Click to buy from Amazon.com or Amazon.co.uk

4. Is It Just Me or Is Everything Shit?: The Encyclopedia of Modern Life.
By Steve Lowe and Alan McArthur. Time Warner Books; 288 pages; £5.99

A broadside against modern culture and the things we love to hate: loft living; bar-clubs; Tony Blair; chick lit; loyalty cards; IKEA; Kabbalah; bling and more.

Click to buy from Amazon.co.uk

5. Team of Rivals: The Political Genius of Abraham Lincoln.
By Doris Kearns Goodwin. Simon & Schuster; 944 pages; $21

How Lincoln won over his fiercest opponents and appointed them to the cabinet.

Click to buy from Amazon.com or Amazon.co.uk

6. Freakonomics: A Rogue Economist Explores the Hidden Side of Everything.
By Steven D. Levitt and Stephen J. Dubner. William Morrow; 256 pages; $17.13. Penguin/ Allen Lane; £8

If you want to know why Roe v Wade may have reduced crime and why drug dealers live with their mothers, this is the book for you.

Click to buy from Amazon.com or Amazon.co.uk

7. Jamie's Italy.
By Jamie Oliver. Michael Joseph; 336 pages; £8

A straight-talking, appetising selection of Italian classics from the telebrity chef.

Click to buy from Amazon.co.uk

8. Rachael Ray 365: No Repeats: A Year of Deliciously Different Dinners.
By Rachael Ray. Clarkson Potter; 352 pages; $13.57

The Food Network darling ensures you can put a different dish on your dinner table every night for a full year in just 30 minutes.

Click to buy from Amazon.com or Amazon.co.uk

9. Teacher Man.
By Frank McCourt. Scribner; 272 pages; $15.60. Fourth Estate; £7.58

Best known for his miserable Irish childhood, Frank McCourt in his third book of memoirs tells of his years as an English teacher in the public high schools of New York City.

Click to buy from Amazon.com or Amazon.co.uk

10. 1776.
By David McCullough. Simon & Schuster; 400 pages; $18.51. Penguin/Allen Lane; £17.50

The rise and fall and rise of George Washington's rebel forces and how they won the day and made history.

Click to buy from Amazon.com or Amazon.co.uk

Global sales from Amazon.com, Amazon.co.uk, Amazon.ca, Amazon.de, Amazon.fr, Amazon.jp, December 1st-23rd 2005. Prices are correct as of January 3rd 2006.

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Obituary

Kerry Packer

Jan 5th 2006
From The Economist print edition

Kerry Francis Bullmore Packer, tycoon and transformer of cricket, died on December 26th, aged 68

BEFORE 1977, the words “cricket” and “commerce” had never been put together. The game belonged to gentlemen and players; sponsorship and long-term contracts were unheard of; the pay was poor. When a young man donned his whites, he was expected to symbolise fair play and national glory, not to earn a decent living. As for the game itself, though it had excitements, the pace of five-day matches could be glacial. The sight of small white figures endlessly regrouping, wandering about, pondering the light, all seen from one fixed angle, made poor spectator sport and even worse television.

So thought Kerry Packer. He was no expert; a huge, brawling, bull-shouldered man, he had been a heavyweight boxer at school and preferred a good game of polo, when he could find a pony strong enough to take him. But as the owner of Channel Nine, Australia's biggest and most successful commercial television network, he wanted to broadcast cricket to the nation, and make it lively. In 1976 he offered the Australian Cricket Board A$1.5m ($1.8m), seven times the usual fee, for exclusive rights to national and international games (“There's a little bit of the whore in all of us, gentlemen. What's your price?”). Astonishingly, they turned him down. So off strode Mr Packer to redesign cricket as he thought it should be.

In World Series Cricket, which ran for two seasons before the ACB caved in, the players wore pink and yellow, and the ball was white. Matches were sometimes played by floodlights at night, to get world audiences. They were often also finished in a day, compressing the action to unbelievable heights of tension and speed. Cameras were put at both ends of the pitch, so that with each ball the batsman could be seen reacting; microphones were fitted on the stumps, to catch the sweet thwack of leather on willow and the thunder of the bowler's feet. Top-rank players, including Tony Greig, then captain of England, and various South Africans, banned from the world game during apartheid, were poached for Mr Packer's teams, where they were treated to good pay and proper contracts. Mr Packer also took the cricketing authorities to court for restraint of trade. The game, though shellshocked, was modernised and professionalised, and has never looked back.

Swashbuckling ruthlessness typified Mr Packer's life. He was an iconoclast, a playboy and a man with an impressive instinct for when to buy, when to sell and when to get nasty. His father, Sir Frank Packer, had amassed an empire that included two TV stations, five radio stations, the *Sydney Daily Telegraph*, nine provincial papers and 60% of the country's magazines. The son, shrewdly building on that basis, rapidly came to dominate Australia physically, financially and commercially.

In 1972, two years before he became chairman, Mr Packer persuaded his father to sell the *Telegraph* to the family's great rival, Rupert Murdoch. He himself, convinced that the future lay with television, not newspapers, pumped the money into Channel Nine. In 1987, at the top of the market, he sold the network to Alan Bond, a financier, for an unheard-of A$1 billion; three years later, he bought it back for a quarter of the price. “You only get one Alan Bond in your life,” he said happily. But 1987 had been a great year; that October, Mr Packer had liquidated his stock holdings just before the market crashed.

A gambling man

He died Australia's richest man, with a fortune of A$7 billion. This was not bad going for a second son with no obvious ability, publicly called “Boofhead” by his father, who had lost two years' schooling with polio and whose first job in the firm had been to shovel newspapers on to the loading machine.

His money was funnelled into ski resorts, casinos, polo ponies, diamond mines, cattle stations, oil, engineering works and vast tracts of land in Queensland and New South Wales. Millions were given, sometimes secretly, to charity; millions were also spread over gambling tables in London and Las Vegas. (Though Mr Packer preferred to stay at home, no Australian casino could handle his wagers.) A three-week losing streak in London was said to have cost him A$28m but, overall, he came up lucky. Life was one big gamble, and a massive heart attack in 1990 had convinced him that “fucking nothing” lay on the other side.

Questions were often asked about the small amounts of tax his companies paid. Mr Packer brushed that off. Canberra was already spending his money so badly that it deserved to get no more. One government commission strayed close to linking him to organised crime, but the attorney-general cleared him. Politicians on both left and right were afraid of him and gave him what he wanted. A rare rebuff, when media cross-ownership laws blocked his designs on the rival Fairfax newspaper empire in 1991, left him furious.

Yet he was not particularly interventionist. His most brutal moment probably came in 1962, when he was sent by his father, with a few mates, to rough up the owner of a Sydney publishing house who was refusing to sell. He was busy trashing the office when Rupert Murdoch, also with a few mates, turned up to fight him. Almost as good as cricket, Packer-style.

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Overview

Jan 5th 2006
From The Economist print edition

The **dollar** suffered its biggest two-day drop against the euro in two years, hitting a two-month low of $1.21 against the European currency on January 4th. The dollar stumbled after the release of the minutes of the December meeting of the Federal Open Market Committee, which signalled that interest-rate rises may be nearing an end.

The index of manufacturing activity published by **America's** Institute for Supply Management fell much more sharply than expected in December, to a four-month low of 54.2. However, that is still consistent with GDP growth of more than 3%.

Some more upbeat figures were published in **Japan** ahead of its new year holiday. The core rate of consumer-price inflation (excluding fresh foods) turned positive (0.1%) in the 12 months to November. This followed more than five years of falling prices apart from a temporary blip in October 2003. However, the overall rate of headline inflation continued to fall at an annual rate of 0.8%. In the same month the unemployment rate rose to 4.6%, but the ratio of job vacancies to applicants rose to 0.99, its highest since 1992. The Nikkei 225 rose to a new five-year high, 42% above its level at the start of 2005.

France's unemployment rate fell by more than expected in November, to 9.6% of its labour force, down from a five-year high of 10.2% in May and its lowest rate since March 2003. **Germany's** official jobless rate fell to 11.2% in December from 12% in March. But on the EU harmonised measure, Germany's rate is much lower, at around 9%.

The average inflation rate in the **euro zone** slowed to 2.2% in the 12 months to December, down from a recent high of 2.6% in September. The growth of M3 money supply also slowed by more than expected, to 7.6% in the year to November. This should ease the concerns of the European Central Bank, but both inflation and money-supply growth remain above the bank's target. The euro area's current-account swung into a deficit of $12 billion in the 12 months to October, compared with a surplus of $52.1 billion a year earlier.

Britain's current-account deficit widened to a record £10.2 billion ($18.2 billion) in the third quarter. The 12-month deficit edged up to $40.6 billion.

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Output, demand and jobs

Jan 5th 2006
From The Economist print edition

% change on year ago

	GDP latest		GDP qtr*	The Economist poll GDP forecasts 2005	2006	Industrial production latest		Retail sales (volume) latest		Unemployment % rate latest		Unemployment % rate year ago
Australia	+ 2.6	Q3	+ 0.6	+ 2.6	+ 3.3	+ 0.7	Q2	+ 1.2	Q3	5.1	Nov	5.2
Austria	+ 1.8	Q3	+ 2.3	+ 1.6	+ 2.0	+ 3.0	Oct	+ 1.3	Oct	5.3	Dec	5.0
Belgium	+ 1.1	Q3	+ 1.7	+ 1.3	+ 1.8	– 7.7	Oct	+ 0.8	Oct	12.8	Nov†	12.8
Britain	+ 1.7	Q3	+ 1.7	+ 1.7	+ 2.1	– 1.8	Oct	+ 2.1	Nov	4.9	Oct††	4.7
Canada	+ 2.8	Q3	+ 3.6	+ 2.9	+ 3.0	+ 1.7	Oct	+ 2.2	Sep	6.4	Nov	7.2
Denmark	+ 4.8	Q3	+ 5.7	+ 2.4	+ 2.4	+ 4.6	Oct	+ 3.5	Nov	5.4	Oct	6.3
France	+ 1.8	Q3	+ 2.8	+ 1.6	+ 1.9	– 1.4	Oct	+ 0.5	Sep	9.6	Nov	10.0
Germany	+ 1.4	Q3	+ 2.5	+ 1.0	+ 1.5	+ 3.8	Oct	– 0.6	Nov	11.2	Dec§	10.8
Italy	+ 0.1	Q3	+ 1.1	+ 0.1	+ 1.2	– 2.7	Oct	+ 0.1	Sep	7.7	Jun	8.1
Japan	+ 2.9	Q3	+ 1.0	+ 2.4	+ 2.2	+ 3.3	Nov	+ 0.4	Oct	4.6	Nov	4.6
Netherlands	+ 1.3	Q3	+ 2.5	+ 0.7	+ 1.8	+ 0.1	Oct	+ 2.7	Sep	6.5	Nov**	6.4
Spain	+ 3.5	Q3	+ 3.3	+ 3.4	+ 3.0	– 0.4	Oct	– 0.2	Oct	8.6	Oct	10.6
Sweden	+ 3.4	Q3	+ 3.9	+ 2.4	+ 2.8	+ 2.5	Oct	+ 9.0	Nov	5.0	Nov†	4.9
Switzerland	+ 2.3	Q3	+ 4.3	+ 1.3	+ 1.8	+ 2.8	Q3	+ 1.6	Sep	3.7	Nov†	3.9
United States	+ 3.6	Q3	+ 4.1	+ 3.6	+ 3.3	+ 2.8	Nov	+ 4.4	Nov	5.0	Nov	5.4
Euro area	+ 1.6	Q3	+ 2.6	+ 1.3	+ 1.8	+ 0.1	Oct	+ 0.4	Oct	8.3	Oct	8.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Finland	+ 1.9	Q3	+12.1	na	na	– 3.4	Nov	+ 5.6	Oct	8.3	Nov	8.7
Greece	+ 3.8	Q3	na	na	na	+ 3.5	Oct	+ 2.6	Oct	9.7	Q3	10.1
Iceland	+ 4.0	Q3	na	na	na	na		na		1.4	Oct†	2.7
Ireland	+ 4.8	Q3	+ 1.3	na	na	+ 0.3	Oct	+ 4.3	Oct	4.3	Nov	4.3
Luxembourg	+ 3.1	Q1	na	na	na	+ 4.9	Sep	+ 1.7	Oct	4.9	Nov	4.4
New Zealand	+ 2.0	Q3	+ 0.2	na	na	– 1.5	Q2	+ 4.9	Q3	3.4	Q3	3.8
Norway	+ 3.1	Q3	+ 3.2	na	na	– 4.1	Oct	+ 3.5	Oct	4.6	Nov**	4.5
Portugal	+ 0.2	Q3	– 3.7	na	na	+ 0.5	Nov	+ 1.1	Nov	7.7	Q3†	6.8

*% change on previous quarter at an annual rate. †Not seasonally adjusted. ††Aug-Oct; claimant count rate 2.9% in Nov. §EU harmonised rate 9.1% in Oct. **Sep-Nov.

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Prices and wages

Jan 5th 2006
From The Economist print edition

% change on year ago

	Consumer prices latest		Consumer prices year ago	The Economist poll consumer prices forecast 2005	2006	Producer prices latest		Producer prices year ago	Wages/earnings latest		Wages/earnings year ago
Australia	+ 3.0	Q3	+ 2.3	+ 2.8	+ 2.8	+ 6.2	Q3	+ 6.1	+ 6.1	Q3	+ 3.5
Austria	+ 1.6	Nov	+ 2.6	+ 2.3	+ 2.0	+ 0.9	Nov	+ 5.6	+ 2.4	Nov	+ 2.0
Belgium	+ 2.9	Dec	+ 2.3	+ 2.5	+ 2.0	+ 1.7	Nov	+ 5.6	+ 2.3	Oct	+ 2.4
Britain	+ 2.1	Nov*	+ 1.5	+ 2.2	+ 2.1	+ 2.3	Nov	+ 3.5	+ 3.6	Oct†	+ 4.2
Canada	+ 2.0	Nov	+ 2.4	+ 2.4	+ 2.4	+ 2.9	Nov	+ 3.8	+ 2.8	Oct	+ 2.0
Denmark	+ 2.0	Nov	+ 1.3	+ 2.0	+ 2.0	+ 3.9	Nov	+ 3.2	+ 2.8	Q3	+ 2.9
France	+ 1.6	Nov	+ 2.0	+ 1.9	+ 1.7	+ 2.8	Nov	+ 3.2	+ 3.2	Q3	+ 2.9
Germany	+ 2.1	Dec	+ 2.1	+ 2.0	+ 1.8	+ 2.2	Nov	+ 4.1	+ 1.0	Oct	+ 2.3
Italy	+ 2.0	Dec	+ 2.0	+ 2.1	+ 2.0	+ 3.7	Nov	+ 4.3	+ 3.0	Nov	+ 2.7
Japan	– 0.8	Nov	+ 0.8	– 0.2	+ 0.3	+ 1.9	Nov	+ 2.1	– 0.3	Nov	+ 3.5
Netherlands	+ 1.8	Nov	+ 1.3	+ 1.5	na	+ 4.5	Nov	+ 5.7	+ 1.1	Nov	+ 0.8
Spain	+ 3.4	Nov	+ 3.5	+ 3.3	+ 3.1	+ 4.9	Nov	+ 5.2	+ 1.9	Q3	+ 2.2
Sweden	+ 0.8	Nov	+ 0.5	+ 0.8	+ 1.6	+ 5.0	Nov	+ 2.9	+ 3.1	Oct	+ 3.8
Switzerland	+ 1.0	Dec	+ 1.3	+ 1.3	+ 1.3	+ 0.8	Nov	+ 1.9	+ 0.9	2004	+ 1.4
United States	+ 3.5	Nov	+ 3.5	+ 3.3	+ 3.1	+ 4.4	Nov	+ 5.2	+ 3.2	Nov	+ 2.4
Euro area	+ 2.2	Dec	+ 2.4	+ 2.2	+ 2.0	+ 4.1	Oct	+ 4.1	+ 2.2	Q3	+ 1.8
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*										
Finland	+ 0.9	Nov	+ 0.5	na	na	+ 4.3	Nov	+ 1.8	+ 3.6	Q3	+ 4.0
Greece	+ 3.5	Nov	+ 3.1	na	na	+ 6.5	Nov	+ 4.0	na		na
Iceland	+ 4.1	Dec	+ 3.9	na	na	+ 3.9	Nov	+ 6.1	+ 7.3	Nov	+ 5.4
Ireland	+ 2.6	Nov	+ 2.9	na	na	+ 3.5	Nov	– 1.6	+ 3.5	Q3	+ 4.7
Luxembourg	+ 2.5	Nov	+ 2.4	na	na	+ 3.0	Oct	+14.6	+ 2.7	Sep	– 0.1
New Zealand	+ 3.4	Q3	+ 2.5	na	na	+ 6.1	Q3	+ 2.5	+ 3.0	Q3	+ 2.2
Norway	+ 1.8	Nov	+ 1.2	na	na	+17.9	Nov	+13.3	+ 2.6	Q3	+ 4.3
Portugal	+ 2.6	Nov	+ 2.5	na	na	+ 3.4	Nov	+ 5.2	– 0.1	Oct	– 2.4

*RPI inflation rate 2.4% in Nov. †Aug-Oct.

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Money and interest rates

Jan 5th 2006
From The Economist print edition

	Money supply* % change on year ago			Interest rates % a year (Jan 4th 2006) 3-mth money market		2-year gov't bonds	10-year gov't bonds		corporate bonds
	narrow	broad		latest	year ago		latest	year ago	
Australia	+ 6.6	+ 8.7	Nov	5.64	5.44	5.18	5.23	5.46	6.18
Britain	+ 5.3	+12.1	Nov	4.58	4.81	4.15	4.09	4.54	5.15
Canada	+ 9.3	+ 8.4	Nov	3.39	2.47	3.71	4.00	4.39	5.09
Denmark	+19.2	+12.2	Nov	2.45	2.25	2.80	3.28	3.78	4.91
Japan	+ 5.5	+ 2.0	Nov	0.02	0.02	0.28	1.52‡	1.40	1.67
Sweden	+ 2.7	+ 7.2	Nov	1.84	2.00	2.51	3.28	3.78	3.32
Switzerland	+ 4.2	+ 6.4	Nov	1.02	0.73	1.68	1.97	2.21	2.24
United States	- 0.2	+ 7.4	Nov	4.22	2.52	4.32	4.36	4.27	5.35
Euro area†	+10.6	+ 7.6	Nov	2.49	2.15	2.80	3.29	3.62	3.75

*Narrow: M1 except Britain and Sweden M0, broad: M2 or M3 except Britain M4. †Germany for bonds. ‡Dec 28th. Benchmarks: US 30-year 4.54%, Japan No. 274 1.44%. Central bank rates: US fed funds 4.25%, ECB refinancing 2.25%, BOJ overnight call 0.001%, BOE repo 4.5%. Sources: Bank of Canada, Commerzbank, Danske Bank, J.P. Morgan Chase, Stockholmsbörsen, UBS, Global Insight, Westpac, Thomson Datastream. Rates cannot be construed as banks' offers.

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The Economist commodity price index

Jan 5th 2006
From The Economist print edition

2000=100

	Dec 20th	Dec 27th	Jan 3rd*	% change on one month	% change on one year
Dollar index					
All items	143.9	146.2	147.1	+ 5.3	+18.5
Food	128.9	131.3	132.9	+ 8.3	+13.4
Industrials					
All	163.3	165.4	165.6	+ 2.4	+24.4
Nfa†	134.6	138.3	139.0	+ 3.8	+15.6
Metals	179.0	180.1	180.0	+ 1.8	+28.5
Sterling index					
All items	124.0	128.0	128.3	+ 5.3	+28.4
Euro index					
All items	111.9	113.9	113.5	+ 3.5	+31.4
Yen index					
All items	156.1	158.8	159.3	+ 1.5	+32.5
Gold					
$ per oz	502.30	501.55	528.70	+ 4.2	+24.1
West Texas Intermediate					
$ per barrel	57.75	57.98	63.10	+ 5.3	+49.6

* Provisional. † Non-food agriculturals.

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Stockmarkets

Jan 5th 2006
From The Economist print edition

Market indices

	Jan 4th	2005-2006 high	2005-2006 low	% change on one week	% change on record high	% change on Dec 31st 2004 in local currency	% change on Dec 31st 2004 in $ terms
Australia (All Ordinaries)	4,765.1	4,765.1	3,905.5	+ 1.4	nil	+17.6	+11.7
Austria (ATX)	3,763.9	3,763.9	2,415.0	+ 3.0	nil	+54.8	+37.7
Belgium (Bel 20)	3,638.5	3,638.5	2,958.8	+ 2.0	- 1.2	+24.1	+10.3
Britain (FTSE 100)	5,714.6	5,714.6	4,783.6	+ 1.6	-17.5	+18.7	+ 8.8
Canada (Toronto Composite)	11,501.5	11,167.2	9,006.2	+ 2.1	nil	+24.4	+29.5
Denmark (OMXCB)	374.2	374.2	257.8	+ 2.0	nil	+45.2	+28.7
France (SBF 250)	3,385.9	3,385.9	2,633.6	+ 1.9	-22.9	+28.5	+14.3
(CAC 40)	4,838.5	4,838.5	3,816.1	+ 1.7	-30.1	+26.6	+12.6
Germany (DAX)*	5,523.6	5,523.6	4,178.1	+ 1.4	-31.5	+29.8	+15.4
Italy (S&P/MIB)	36,336.0	36,336.0	30,645.0	+ 1.3	-27.5	+17.6	+ 4.6
Japan (Nikkei 225)	16,361.5	16,361.5	10,825.4	+ 1.0	-58.0	+42.4	+25.5
(Topix)	1,673.1	1,673.1	1,109.2	+ 1.2	-42.0	+45.5	+28.2
Netherlands (AEX)	445.0	445.0	347.0	+ 1.3	-36.6	+27.8	+13.7
Spain (Madrid SE)	1,175.5	1,176.9	950.9	+ 1.4	- 0.1	+22.6	+ 9.0
Sweden (Affarsvarlden Gen)	296.9	296.9	218.9	+ 1.3	-25.8	+34.2	+15.4
Switzerland (Swiss Market)	7,723.7	7,723.7	5,669.6	+ 2.2	- 8.2	+35.7	+20.4
United States (DJIA)	10,880.2	10,940.6	10,012.4	+ 0.8	- 7.2	+ 0.9	+ 0.9
(S&P 500)	1,273.5	1,272.7	1,137.5	+ 1.2	-16.6	+ 5.1	+ 5.1
(NASDAQ Comp)	2,263.5	2,273.4	1,904.2	+ 1.5	-55.2	+ 4.0	+ 4.0
Europe (FTSEurofirst 300)†	1,301.5	1,301.5	1,038.6	+ 1.8	-23.7	+24.9	+11.1
Euro area (FTSE Euro 100)†	1,111.6	1,111.6	894.4	+ 1.4	-28.3	+23.4	+ 9.7
World (MSCI)‡	1,295.1	1,295.0	1,115.0	+ 2.1	-10.6	+10.8	+10.8
World bond market (Citigroup)††	631.8	662.3	608.7	+ 1.3	- 4.6	- 5.2	- 5.2

*Total return index. †In euro terms. ‡Morgan Stanley Capital International Index includes individual markets listed above plus eight others, in $ terms. ††Citigroup World Government Bond Index, total return, in $ terms.

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Trade, exchange rates and budgets

Jan 5th 2006
From The Economist print edition

	Trade balance*, $bn latest 12 months		Current-account balance $bn latest 12 mths		The Economist poll % of GDP, forecast 2005	2006	Exchange rate trade-weighted† 2000=100 Jan 4th	year ago	Currency units per $ Jan 4th	year ago	per £	per euro	per ¥100	Budget balance % of GDP 2005‡
Australia	− 15.3	Oct	− 43.5	Q3	− 5.9	− 5.3	117.4	113.0	1.34	1.30	2.36	1.62	1.15	+ 1.0
Austria	− 1.8	Oct	− 0.1	Oct	nil	− 0.2	103.8§	104.4	0.83	0.75	1.46	–	0.71	− 2.0
Belgium	+ 16.1	Oct	+ 9.2	Jun	+ 2.3	+ 2.3	104.3§	105.1	0.83	0.75	1.46	–	0.71	nil
Britain	−115.5	Oct	− 40.6	Q3	− 1.7	− 1.9	98.1	98.9	0.57	0.53	–	0.69	0.49	− 3.1
Canada	+ 50.9	Oct	+ 19.6	Q3	+ 1.6	+ 1.6	126.1	116.4	1.15	1.22	2.02	1.39	0.99	+ 1.3
Denmark	+ 10.0	Oct	+ 9.7	Oct	+ 2.9	+ 2.6	105.9	106.9	6.17	5.60	10.9	7.46	5.31	+ 2.8
France	− 28.9	Oct	− 31.4	Oct	− 1.1	− 0.9	106.8§	107.7	0.83	0.75	1.46	–	0.71	− 3.2
Germany	+202.9	Oct	+113.6	Oct	+ 3.9	+ 3.7	104.6§	105.5	0.83	0.75	1.46	–	0.71	− 3.9
Italy	− 11.2	Oct	− 28.3	Oct	− 1.4	− 1.5	76.5§	77.1	0.83	0.75	1.46	–	0.71	− 4.3
Japan	+ 98.2	Oct	+164.3	Oct	+ 3.3	+ 3.3	82.4	89.0	116	104	205	141	–	− 6.5
Netherlands	+ 39.3	Oct	+ 44.3	Q3	+ 4.2	+ 4.2	103.8§	104.6	0.83	0.75	1.46	–	0.71	− 1.6
Spain	− 93.9	Sep	− 79.0	Aug	− 6.0	− 5.7	77.2§	77.6	0.83	0.75	1.46	–	0.71	+ 0.3
Sweden	+ 20.3	Nov	+ 24.2	Q3	+ 7.1	+ 6.5	96.1	101.2	7.73	6.80	13.6	9.35	6.65	+ 1.2
Switzerland	+ 7.0	Oct	+ 51.4	Q2	+12.5	+12.0	106.8	107.9	1.28	1.17	2.25	1.55	1.10	− 1.6
United States	−767.8	Oct	−780.6	Q3	− 6.5	− 6.5	86.1	81.2	–	–	1.76	1.21	0.86	− 3.7
Euro area	+ 41.8	Oct	− 12.0	Oct	+ 0.1	+ 0.1	116.3	119.9	0.83	0.75	1.46	–	0.71	− 2.9
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*													
Finland	+ 11.6	Oct	+ 7.3	Oct	na	na	81.4§	81.9	0.83	0.75	1.46	–	0.71	+ 2.1
Greece	− 34.3	Oct	− 17.0	Oct	na	na	59.9§	60.2	0.83	0.75	1.46	–	0.71	− 4.5
Iceland	− 1.5	Nov	− 2.2	Q3	na	na	106.7**	96.6	61.8	62.6	109	74.7	53.1	+ 2.0
Ireland	+ 40.5	Oct	− 3.7	Q3	na	na	94.0§	95.2	0.83	0.75	1.46	–	0.71	− 0.9
Luxembourg	− 4.5	Sep	+ 3.5	Q2	na	na	104.3§	105.1	0.83	0.75	1.46	–	0.71	− 2.3
New Zealand	− 4.6	Nov	− 9.1	Q3	na	na	137.3	131.8	1.45	1.42	2.55	1.75	1.25	+ 5.3
Norway	+ 46.0	Nov	+ 43.7	Q3	na	na	110.1	106.3	6.57	6.23	11.6	7.94	5.65	+ 15.3
Portugal	− 14.2	Aug	− 16.6	Oct	na	na	93.4**	93.6	0.83	0.75	1.46	–	0.71	− 6.0

*Merchandise. Australia, Britain, France, Canada, Japan and United States imports fob, exports fob. All others cif/fob. †Bank of England except §IMF, October average. ‡OECD estimate. **IMF, August average.

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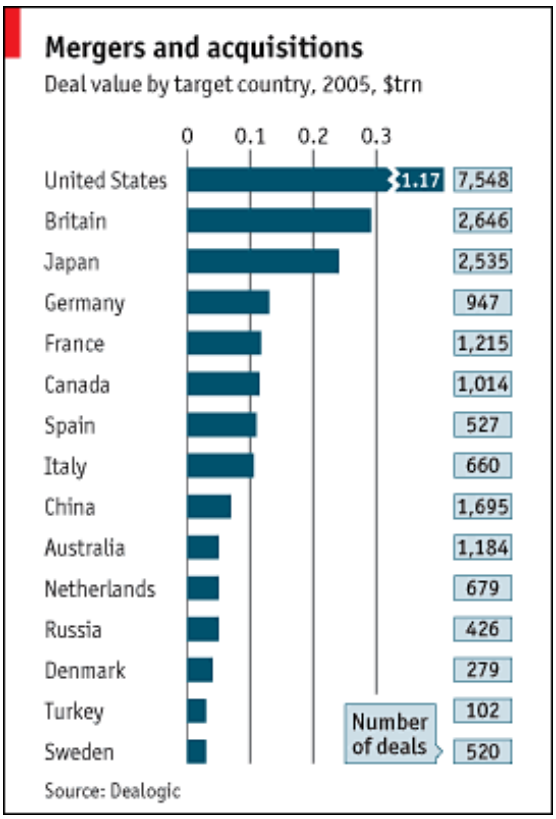
Mergers and acquisitions

Jan 5th 2006
From The Economist print edition



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Overview

Jan 5th 2006
From The Economist print edition

Indicators for **Saudi Arabia** and **Pakistan** are included on these pages for the first time this week. Both economies are doing well. Saudi Arabia grew by 6.2% in 2005, according to estimates by the Economist Intelligence Unit. Pakistan grew by 8.4% in the past financial year, ending in June.

Inflationary pressure is building in **India**. Consumer prices rose by 5.3% in the year to November, the fastest rate since 2000.

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Stockmarkets

Jan 5th 2006
From The Economist print edition

In 2005 Egypt had the best-performing stockmarket among those tracked by *The Economist*, with a gain of 125% in dollar terms. The worst performer was in Venezuela, where share prices fell by more than 30%. Share prices also fell in China (for the second year in a row) and Malaysia. The 3% gain in the S&P 500 ranked it 38th out of 42.

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Economy

Jan 5th 2006
From The Economist print edition

	% change on year ago						Latest 12 months, $bn				Foreign reserves* $bn, latest	
	GDP		Industrial production		Consumer prices		Trade balance		Current account			
China	+ 9.4	Q3	+16.6	Nov	+ 1.3	Nov	+102.1	Nov	+128.5	H1 2005	769.0	Sep
Hong Kong	+ 8.2	Q3	+ 4.1	Q3	+ 1.7	Nov	– 9.4	Nov	+21.0	Q3	122.4	Nov
India	+ 8.0	Q3	+ 8.5	Oct	+ 5.3	Nov	–37.3	Nov	–18.3	Q3	136.0	Nov
Indonesia	+ 5.3	Q3	– 5.9	Oct	+17.1	Dec	+26.2	Nov	+ 0.7	Q3	31.7	Nov
Malaysia	+ 5.3	Q3	+ 4.4	Oct	+ 3.5	Nov	+25.6	Nov	+18.7	Q3	72.5	Nov
Pakistan	+ 8.4	2005†	+11.0	Jun	+ 7.9	Nov	– 8.9	Nov	– 3.7	Q3	9.6	Nov
Philippines	+ 4.1	Q3	+ 4.6	Oct	+ 6.6	Dec	– 2.2	Oct	+ 2.9	Sep	15.5	Nov
Singapore	+ 7.7	Q4	+22.4	Nov	+ 1.0	Nov	+17.3	Nov	+33.7	Q3	114.9	Nov
South Korea	+ 4.5	Q3	+12.2	Nov	+ 2.6	Dec	+23.5	Dec	+18.1	Nov	208.2	Nov
Taiwan	+ 4.4	Q3	+ 9.0	Nov	+ 2.5	Nov	+ 3.8	Nov	+ 8.9	Q3	251.8	Nov
Thailand	+ 5.3	Q3	+ 5.0	Nov	+ 5.8	Dec	– 8.0	Nov	– 3.2	Nov	49.4	Nov
Argentina	+ 9.2	Q3	+ 7.5	Nov	+12.0	Nov	+11.1	Nov	+ 4.4	Q3	25.7	Oct
Brazil	+ 1.0	Q3	+ 0.4	Oct	+ 6.2	Nov	+44.8	Dec	+14.9	Nov	64.3	Nov
Chile	+ 5.2	Q3	+ 6.2	Nov	+ 3.6	Nov	+ 9.2	Nov	– 0.2	Q3	16.0	Nov
Colombia	+ 5.8	Q3	+ 0.5	Oct	+ 4.9	Dec	+ 1.5	Sep	– 1.7	Q3	14.6	Nov
Mexico	+ 3.3	Q3	+ 2.6	Oct	+ 2.9	Nov	– 8.6	Nov	– 8.4	Q3	71.2	Oct
Peru	+ 7.2	Oct	+ 4.1	Oct	+ 1.5	Dec	+ 4.4	Oct	+ 0.8	Q3	12.6	Nov
Venezuela	+ 9.8	Q3	+10.8	Oct	+14.4	Dec	+28.2	Q3	+21.6	Q3	24.4	Oct
Egypt	+ 5.2	Q1	+ 4.0	2005†	+ 3.4	Nov	–10.4	Q2	+ 2.9	Q2	19.8	Oct
Israel	+ 5.7	Q3	–15.2	Oct	+ 2.7	Nov	– 7.8	Nov	+ 2.4	Q3	28.1	Nov
Saudi Arabia	+ 6.2	2005‡	na		+ 0.4	Aug	+84.6	2004	+51.9	2004	29.8	Oct
South Africa	+ 4.9	Q3	+ 0.3	Oct	+ 3.4	Nov	– 3.4	Nov	–10.3	Q3	17.9	Nov
Czech Republic	+ 4.9	Q3	+ 6.3	Oct	+ 2.4	Nov	+ 1.5	Oct	– 3.4	Q3	29.2	Nov
Hungary	+ 4.5	Q3	+ 9.8	Oct	+ 3.3	Nov	– 3.5	Oct	– 8.7	Q3	16.7	Nov
Poland	+ 3.7	Q3	+ 8.5	Nov	+ 1.0	Nov	– 3.0	Oct	– 4.5	Oct	39.9	Nov
Russia	+ 7.0	Q3	+ 5.5	Nov	+10.4	Nov	+119.6	Oct	+87.4	Q3	164.7	Nov
Turkey	+ 7.0	Q3	+ 7.0	Oct	+ 7.7	Dec	–43.2	Nov	–22.1	Oct	47.9	Nov
MORE COUNTRIES	Data for the countries below are not provided in printed editions of *The Economist*											
Estonia	+10.8	Q3	+ 8.7	Oct	+ 3.9	Nov	– 2.4	Sep	– 1.4	Oct	1.9	Oct
Latvia	+11.4	Q3	+ 5.8	Oct	+ 7.4	Nov	– 2.9	Oct	– 1.8	Oct	2.3	Oct
Lithuania	+ 7.6	Q3	na		+ 2.8	Nov	– 3.5	Oct	– 1.6	Oct	3.7	Oct
Slovakia	+ 6.2	Q3	+ 4.5	Oct	+ 3.4	Nov	– 1.9	Oct	– 2.6	Aug	15.1	Oct
Slovenia	+ 3.7	Q3	+ 2.8	Oct	+ 2.1	Nov	– 1.5	Oct	+ 0.1	Oct	8.2	Sep

*Excluding gold, except Singapore; IMF definition. †Year ending June. ‡Economist Intelligence Unit estimate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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Financial markets

Jan 5th 2006
From The Economist print edition

	Currency units			Interest rates	Stockmarkets	% change on		
	per $		per £	short-term	Jan 4th		Dec 31st 2004	
	Jan 4th	year ago	Jan 4th	% a year		one week	in local currency	in $ terms
China	8.07	8.28	14.2	2.50	1,241.9	+2.1	– 6.6	– 4.2
Hong Kong	7.75	7.79	13.6	4.20	15,200.1	+0.7	+ 6.8	+ 7.1
India	44.7	43.7	78.7	6.09	9,648.1	+4.2	+ 46.1	+ 42.0
Indonesia	9,655	9,310	16,990	14.46	1,211.7	+4.1	+ 21.1	+ 16.5
Malaysia	3.77	3.80	6.64	3.26	897.1	+0.2	– 1.1	– 0.4
Pakistan	59.79	59.40	105.21	8.72	9,853.7	+4.1	+ 58.5	+ 57.4
Philippines	52.3	56.2	92.1	6.75	2,138.1	+3.4	+ 17.3	+ 25.8
Singapore	1.65	1.65	2.90	3.25	2,384.1	+2.0	+ 15.4	+ 14.5
South Korea	998	1,046	1,757	4.12	1,402.1	+2.5	+ 56.5	+ 62.3
Taiwan	32.3	31.9	56.9	1.65	6,614.4	+1.4	+ 7.7	+ 5.6
Thailand	40.5	39.1	71.2	4.50	743.2	+5.4	+ 11.2	+ 6.7
Argentina	3.04	2.97	5.35	9.13	1,610.5	+4.7	+ 17.1	+ 14.5
Brazil	2.31	2.70	4.06	17.98	35,002.0	+5.6	+ 33.6	+ 53.8
Chile	515	564	907	5.28	9,330.8	+2.4	+ 4.1	+ 12.3
Colombia	2,282	2,343	4,016	6.19	9,540.7	+1.7	+119.5	+126.3
Mexico	10.6	11.3	18.6	7.98	18,669.2	+5.5	+ 44.5	+ 52.2
Peru	3.44	3.27	6.05	3.56	4,911.5	+1.8	+ 32.4	+ 26.2
Venezuela	2,557§	2,702§	4,500	10.37	20,246.0	+0.2	– 32.4	– 31.9
Egypt	5.74	5.96	10.10	8.57	57,270.7	+4.4	+133.0	+146.4
Israel	4.58	4.38	8.06	4.75	856.4	+4.7	+ 33.0	+ 25.5
Saudi Arabia	3.75	3.75	6.60	4.97	17,499.0	+4.6	+113.2	+113.2
South Africa	6.16	5.93	10.8	7.15	18,415.3	+1.9	+ 45.5	+ 33.1
Czech Republic	24.0	22.9	42.2	2.20	1,496.1	+2.3	+ 45.0	+ 35.0
Hungary	207	185	365	6.23	21,698.7	+4.9	+ 47.2	+ 28.3
Poland	3.16	3.10	5.56	4.56	37,631.2	+5.0	+ 41.3	+ 33.9
Russia	28.7	27.9	50.6	12.00	1,125.6‡	+0.9	+ 90.0	+ 83.3
Turkey	1.34	1.35	2.35	14.86	41,362.5	+5.5	+ 65.6	+ 67.1
EM (MSCI)*	1.00	1.00	1.76	na	734.9	+6.7	+ 35.6	+ 35.6
EMBI+†	1.00	1.00	1.76	na	371.5	+2.6	+ 12.7	+ 12.7

*Emerging Mkts. †J.P. Morgan Chase's Emerging Mkts Bond Index Plus. ‡In $ terms. §Floating exchange rate.

Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; Hong Kong Monetary Authority; Centre for Monitoring Indian Economy; Bank Leumi le-Israel; Standard Bank Group

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